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THE UNITED STATES

by

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I. INTRODUCTION

The purpose of this memorandum is to state the status of seven specified types of activity under the American antitrust laws. Since the exposition is intended to be relevant to development of policy in another country, it will be limited to the parts of the American laws that are generally applicable. It will disregard special types of application that depend not only upon the nature of the antitrust laws but also upon the nature of other types of legislation, applicable to certain aspects of the economy, that establish special exemptions or regulations limited to these aspects; for in such instances American experience would be relevant to the legislative problems of another country only if that country's regulatory legislation resembled that of the United States.

Thus this memorandum will ignore the interaction between the anti-trust laws and,

- the laws that validate monopoly rights for patents and copyrights;

- the regulatory laws that are applicable to common carriers, public utilities, banks, etc.;

- the laws that grant partial exemption from the antitrust laws to particular economic groups, such as farmers;

- the laws that partially subordinate antitrust policy to the policies of the individual American states, as in the case of insurance and resale price maintenance;

- various statutory exemptions and grants of special protection that are narrowly

applicable to particular problems (e.g., the provisions of law as to motor vehicle franchises);

- certain exemptions that may be granted under the Defense Production Act of 1950.

Similarly, except as to the Export Trade Act, this memorandum will discuss only application of the antitrust laws to conduct and business organization within the United States. It will disregard so-called "extra-territorial" applications of the American laws.

For purposes of this memorandum, the antitrust laws will be considered to consist of the Sherman Act, those parts of the Clayton Act that are not concerned with common carriers and banks, the Federal Trade Commission Act, and the statutes by which these laws, except in the respects already mentioned, have been amended as to substance or supplemented as to procedures and remedies. They will not be considered to include the antitrust provisions of other statutes (e.g., the Wilson Tariff Act), which, in general, have application limited to particular segments of activity or convey limited authority to particular official bodies. General familiarity with the provisions of the antitrust laws will be presumed in the body of the memorandum, though particular provisions will be mentioned there when relevant; but the content of the statutes and the nature of the procedures by which they are applied will be summarized in an appendix.

II. SPECIALIZATION AGREEMENTS

A specialization agreement is one by which two or more business enterprises (almost always manufacturers) agree that each of them will produce only specified products or types of product. Usually the agreement includes provisions by which each party will sell its specialized products to the other party, so that in selling to non-participants each can offer a full line of the products. Under the laws of some countries, such agreements are considered permissible means by which the parties can achieve economies from greater specialization and longer production runs.

The American antitrust laws treat such agreements as allocations of types of product in which each participant undertakes to refrain from producing products made by the others and thereby participates reciprocally in limiting competition. If such an agreement involved non-trivial amounts of trade and affected interstate commerce, it would be illegal under Section 1 of the Sherman Act. Even patent rights and judicial recognition that technological necessity often justifies the cross-licensing of patents do not protect a contractual allocation of products by which competition among the parties is foreclosed and entry by other competitors is prevented.[1] Similarly, under Section 5 of the Federal Trade Commission Act such an agreement would be illegal as an unfair method of competition.

The economies that, in some countries, are considered to be benefits that can justify such an agreement would have little chance to save it in the United States, for two reasons. First, agreement is not considered necessary to achieve the relevant economies. If specialization promises substantial economy, a single enterprise can specialize by individual

action more easily and quickly than by first inducing others to join it in an allocation agreement. The economies attained by the specialist enhance his competitive opportunities by enabling him to reduce his prices. If he wishes to continue to offer to buyers goods additional to those that he produces, he usually can buy such goods at wholesale, and can protect his future access to such goods by long-term contracts, without needing to promise that he will abstain from producing the goods or to require that his suppliers promise to abstain from producing his specialty. Thus, in practice, specialization unsupported by allocation agreements is common. If access to complementary goods is restricted (except under a patent or other legally sanctioned control), the restriction probably indicates concerted restriction by producers of the withheld goods, as to which an appropriate antitrust corrective should be applied.

Secondly, even if economies not otherwise attainable could be achieved by a specialization agreement, they would be unlikely to be legal justification for the agreement. Though under Section 5 (b) of the Federal Trade Commission Act the Commission acts only if it thinks "that a proceeding by it...would be in the interest of the public," the proceedings under Section 1 of the Sherman Act are not similarly discretionary. The statute declares illegal every contract, combination, or conspiracy in restraint of trade among the states; and in applying the law, though the judges may consider whether or not such an agreement is truly restrictive, they do not have the authority to consider whether or not a restrictive agreement is in the public interest. Exemption of specialization agreements from the Sherman Act would

require statutory action by the Congress, not merely judicial action by the courts.

Proceedings against specialization agreements have been practically non-existent in the United States except in a context of patent licensing, apparently because except in that context such agreements seldom exist. If the purpose of enterprises is to reduce competition among themselves, and if, without patents, they are sufficiently few and sufficiently protected against new competitors to make allocation practicable, they can allocate in ways that are more flexible and more easily concealed than by allocating products. By allocating territories or customers, they can make their division of fields less obvious, their commitments about the future less rigid, and readjustment of these commitments as conditions change less difficult. Perhaps for such reasons, the allocation agreements independent of patents that have come to government attention usually have been of these other types. [2]

II SPECIALIZATION AGREEMENTS

Footnotes

1. See Hartford-Empire Co. v. U.S., 323 U.S. 386.

2. In discussing division of markets among competitors, the 1955 report of the Attorney General's Antitrust Committee focussed its attention upon allocation of territories and of customers, without specific attention to allocation of products. It noted the dependence of such agreements upon conditions in which companies are few and possess substantial, usually dominant, market power. It cited such precedents as the Supreme Court's decisions in 1899 in Addyston Pipe and Steel Co. v. U.S., 175 U.S. 211, and in 1951 in Timken Roller Bearing v. U.S., 341 U.S. 593, and concluded that, though no Supreme Court case had rested on market division alone, there was little doubt, either as a matter of principle or of precedent, that agreement among competitors for market division should be and would be treated like price control agreements (which are illegal *per se*).

III. EXPORT AGREEMENTS

Since 1918, export trade agreements have received special treatment under a special statute. This law, the Export Trade Act (sometimes called the Webb-Pomerene Act) was intended to promote export trade. It rested on the belief that American exporters often encounter strong combinations of foreign competitors or foreign buyers, and strong transportation enterprises, with which they cannot cope individually, and that such exporters are often too small to attain individually the economies possible if they act together. [1]

The Act exempts from the Sherman Act, subject to specific conditions, associations limited to export trade and agreements and acts by them in the course of such trade. The limiting conditions are that the association, agreement, or act is not "in restraint of trade within the United States" and is not "in restraint of the export trade of any domestic competitor of such association"; and that the association does not " either in the United States or elsewhere, enter into any agreement, understanding or conspiracy, to do any act which artificially or intentionally enhances or depresses prices within the United States of commodities of the class exported by such association, or which substantially lessens competition within the United States or otherwise restrains trade therein."

The Act also exempts from the Clayton Act acquisition or ownership by any corporation of stock in a corporation solely engaged in export trade unless the effect may be "to restrain trade or substantially lessen competition within the United States."

These exemptions are qualified by the Federal Trade Commission Act's provisions about unfair methods of competition which cover such methods when used in export trade against a competitor engaged in export trade "even though the acts constituting such unfair methods are done without the territorial jurisdiction of the United States" -- a claim of jurisdiction which was regarded in 1918 as controversial.

The Act provides for surveillance by the Commission over the exempted associations. To this end, it requires each association to register with the Commission, to furnish lists of members and the documents that create its structure (articles of incorporation and by-laws for corporations, contracts of association for others), to give notice annually of changes in these, and to furnish "such information as the Commission may require as to its organization, business, conduct, practices, management, and relation to other associations, corporations, partnerships, and individuals." Failure to provide the required information deprives the association of its exemptions and also is subject to civil penalties of $100 per day.

The Act gives the Commission authority to investigate associations and, upon concluding that the law has been violated, to "make to such association recommendations for the readjustment of its business, in order that it may thereafter maintain its organization and management and conduct its business in accordance with law." Instead of empowering the Commission to enforce its recommendations, however, the Act provides that if an association does not comply with the recommendations, the Commission shall refer its findings and recommendations to the Attorney General "for such action thereon as he may deem proper."

Though the statute has not been changed since 1918, its interpretation by the Commission has been substantially altered. Assuming that export associations would buy their members' products and resell them, the Commission at first told associations which limited themselves to fixing export prices for their members, or otherwise performed limited export functions, that they did not qualify for exemption.[3] Legislation to change this interpretation was repeatedly proposed but not adopted. In 1924, however, the Commission, acting by a vote of three to two, changed its interpretation substantially in a published letter that replied to inquiries by certain producers of silver.[4] The Commission thought that the exemptions did not cover re-export of foreign goods or sale of goods produced abroad by members of an export association. As to goods produced in the United States, it held, however, that the Act does not require an association to perform all the functions of selling members' products to foreign buyers, but that an association may limit itself to such activities as "allotting export orders among its members" and "fixing prices at which the individual members shall sell in export trade." The Commission thought that the Act's "sole purpose was the lessening of competition between domestic exporters in the foreign markets."

As to effects on domestic prices, this letter said that: "The mere fact that there was a rising price in the domestic market would not be a controlling element. It is perfectly apparent that the proper adjustment of distribution may result in an increase in price in a glutted market and a decrease in price in one which is insufficiently supplied. Manifestly, the arrangement must be devoid of any concerted curtailment of production or withdrawal from the domestic market of any part of its normal supply.

It is well understood that an incidental or inconsequential effect upon domestic prices is not unlawful. If a merely consequential rise in price should bar American Exporters from using this statute, the statute might become a nullity. The statute provides for a lawful course of procedure, and if this procedure is followed and the statute complied with, merely indirect or consequential results cannot be held to be against the law."

Moreover, the letter specifically authorized arrangements by export associations with foreign enterprises about foreign markets: "...there seems to be no reason why a Webb-Pomerene association composed of nationals or residents of the United States and actually exporting from the United States, might not adopt a trade arrangement with non-nationals reaching the same market, providing this market was not the domestic market of the United States and the action of this organization did not reflect unlawfully upon domestic conditions."

The interpretation by which the export exemption is available for associations with limited export functions, including functions limited to imposing restrictions upon export sales by members, is still in effect.

However, in other respects the silver letter has been replaced by less permissive interpretations of the exemption. In the period 1940-1950, three developments contributed to the change.

First, the Department of Justice undertook proceedings against export agreements under the Sherman Act. An initial case against the Alkali Export Association resulted in decision by the Supreme Court that the Department could act without waiting for a reference from the Commission [5] and subsequently, after trial on

the merits, in a judgment against the association.[6] In two other similar proceedings, the Electrical Apparatus Export Association was dissolved by consent decree in 1947,[7] and Minnesota Mining and Manufacturing Company was subjected to a corrective order in 1950.[8] These cases under the Sherman Act made clear some of the limits of the exemption. In the Alkali case the court held that associations cannot agree with foreign cartels to allocate markets. Moreover, it found that the association had tried to stabilize domestic prices by exporting the part of the supply considered surplus, and held that such a policy "finds no sanction in the Webb Act and must be condemned under the Sherman Act." The decision in the Minnesota Mining case held that export of capital is not export trade, and so condemned association programs for acquisition of foreign productive facilities. It recognized, however, that, though every export association, inevitably has a restrictive effect upon domestic trade, "if there are only these inevitable consequences an export association is not an unlawful restraint."

Secondly, the Federal Trade Commission launched a series of investigations. A preliminary look at 58 associations resulted in 45 informal investigations between 1943 and 1951, eight of which resulted in recommendations as to readjustment of practices.[9] These court cases and Commission proceedings, taken together, found violations of the limits of the exemption by 11 associations. They included instances in which five associations agreed with foreign cartels and foreign competitors, six associations restrained American exports, two associations directly restrained domestic competitors, and one association restrained imports into the United States.[10]

Thirdly, in an atmosphere of growing concern about international cartels, the Commission published reports that set forth in considerable detail the ties between export associations and such cartels in five product fields, phosphates, copper, sulphur, steel, electrical equipment, and potash.[11]

These developments were followed in 1955-56 by public statements that superseded much of the silver letter. A release by the Commission in 1955 said "that price fixing arrangements with foreign competitors cannot be considered exempted by the Webb-Pomerene Export Trade Law from anti-trust consideration under the Sherman Act," and that such agreements would not be considered to be in the course of export trade within the meaning of that Act. The statement said that one association had been told that continuance of its price-fixing arrangement with its chief foreign competitor would result in reference of the matter to the Department of Justice.[12] In the following year the Commission further tightened its interpretation of the limits of the law by releasing a digest of an advisory opinion which included the statement that: "While membership in a Webb-Pomerene association by firms owning foreign affiliates is permissible, the statutory exemption enjoyed by the association is lost if artificial or intentional enhancement or depression of domestic prices is in any way traceable to the foreign operations of member firms." It noted that in the case at issue, foreign plants owned by association members were sending "a substantial proportion" of their output to the United States and thereby supplying "a substantial share" of the domestic consumption.[13]

The interpretations thus released in 1955 and 1956 are still in effect. The Commission has made available to associations mimeographed lists of activities "prohibited" and "permitted". The "permitted" activities are described as those which on past occasions, in particular situations in which they have occurred, have been deemed not unlawful by the Commission or the courts. The "prohibited" activities are those which, on one or more occasions, have been subjects of an adverse recommendation by the Commission or an adverse order by a court. In both lists, the instances cited all pertain to the period 1940-1950.

The lists may be regarded as the Commission's summation of the content and limits of the exemption so far as these have been decided in practice and can be stated without stating the facts of particular environmental settings. The prohibitions listed also provide further detail about types of violation that have been encountered. Since the lists were derived from particular cases over a 10-year period, certain overlaps and apparent inconsistencies appear in them that deprive them of full coherence.

The lists are reproduced below, with the references to particular cases omitted.

Permitted

The following acts and practices have been considered on one or more occasions and deemed lawfully to comply with the objective of the Act, viz., to permit expanded export trade:

1. Promulgation of rules or regulations providing that all export sales of members are to be made exclusively through the association, even tough members of the

association account for a large percentage of the industry.

2. Promulgation of rules reasonably restricting members' right to withdraw from the association and restricting for a limited period their right after withdrawal to compete with the association in export trade.[14]

3. An association can fix prices and terms of sale of exports of all members whether it functions by purchase or resale of members' products on its own account, or operates by taking and placing orders for export sales on behalf of members.

4. An association can, by itself or in conjunction with cartels, allocate exclusive trade areas if, but only if, the United States and its territories and possessions are excluded from the agreement.[15]

5. An association can assign quotas on exports by its members.

6. An association can select its own distributors or brokers and refuse to sell to additional or alternative brokers or dealers.

Prohibited

1. The following prohibitions have been imposed on the ground that the association had violated the Webb-Pomerene Act by improperly restraining exports by domestic producers:

A.) Associations have been prohibited from entering into any understanding or agreement of any kind with domestic producers who are not regularly admitted

and recognized members of the association with respect to prices, terms of sale, or understandings whereby the non-members were in any manner to refrain from competing with the association. This prohibition plainly includes agreements by an association to sell the products of non-members, which thereby permit the association to fix non-members' export prices.

B.) Associations have been prevented from entering into any agreement or understanding whereby the exports of domestic non-member producers are to be deducted from the export quota of the association.

C.) Associations have been prohibited from entering into any agreements which tend to curtail American exports by prohibiting members from selling to domestic exporters who might compete with the association, or from requiring that all sales by members within the United States be deducted from their export quotas in the association.

D.) An association has been prohibited from falsely representing that it is the sole export representative of the United States in a given industry.

E.) Associations have been prohibited from entering into an agreement with the owners and operators of a shipping terminal to restrict and confine use of the terminal to members of the association.

F.) An association has been prohibited from acquiring control, or participating in any plan to acquire control, of any patent or process useful in the production of the goods it markets. (In this instance it appeared that the purpose of the acquisition of the patent was merely to hold the patent as a

defensive measure to prohibit its use by others.)

G.) An association has been prohibited from entering into any agreement precluding or in any way restricting the right of the association or its members from using a trademark or label within the United States.

2. The following prohibitions have been entered against practices restricting the right of domestic producers to compete within the United States:

A.) Associations have been prohibited from entering into any agreements whereby they controlled or attempted to control any of the terms or conditions of sale by members within this country.

B.) An association has been prohibited from entering into any agreements with members whereby sales by members within the United States are deducted from the export quotas of such companies.

3. The following prohibitions have been entered against practices said to unlawfully restrict actual or potential imports into the United States, or its territories or possessions:

A.) Associations have been prohibited from fixing prices, terms, discounts, or other conditions of sale by members or non-members in any territory or possession of the United States.

B.) Associations have been prohibited from entering into agreements or understandings with any foreign producer, producers, or

cartels whereby the United States is designated as an exclusive trade area, or imports into the United States are otherwise curtailed or restricted.

C.) Associations are not permitted, either themselves or through subsidiaries, to own, operate, or own stock in corporations or other producers outside the United States, if there is any possibility that the markets supplied by such foreign operations might, in the absence of such companies, be supplied by exports from the United States.

4. An association has been prevented from entering into an understanding or agreement whereby foreign producers were guaranteed the right to sell within a given area a specified minimum tonnage over and above sales in that area by the association.

5. An association has been prohibited from entering into or continuing rules, contracts, or agreements discriminating between its members as to the right of withdrawal or resignation, or restricting the right of the former member to compete with the association after withdrawal.

6. An association has been prohibited from conducting its office operations jointly with a domestic trade association and has been required to retain independent office personnel.

7. An association has been prohibited from entering into a general agreement, understanding, or contract to "maintain the status quo" in the world market in the industry and to do nothing which would encourage any change in the competitive trade situation in the industry.

8. An association has been prohibited from obtaining agreements from its members which unreasonably restricted the right of members to withdraw from the association, and were required to replace these with reasonable withdrawal provisions.

9. An association has been prevented from taking into its membership any foreign purchaser or customer or any representative or affiliate of any such foreign company.

In 1963 the Commission began to exercise closer surveillance over export associations. It established in the office of its general counsel an export trade division. Thereafter each association was expected to file annually answers to a questionnaire about its activities and to give the Commission copies of the minutes of its meetings. Though there have been subsequent legal proceedings involving associations, these have been concerned with new developments about which the meaning of the exemption was not clear.

The question central to the recent cases has been whether or not the exemption applies to sales abroad when these are made to the American government or to foreign buyers who use funds supplied by that government. The answer is no. Two cases have involved the problem. Restrictions by a phosphate export association applied to Korean purchases made with funds from an American government assistance program resulted in a proceeding against the association under the Sherman Act. After the suit was filed, the American agency that supplied the funds changed its rules, so that export associations may not bid on contracts financed by it where Americans only may bid; and thereupon the association

was dissolved. Nevertheless, the case reached the Supreme Court, which held that the export exemption was not applicable. "The burden of non-competitive pricing falls, not on any foreign purchaser, but on the American taxpayer. The United States was, in essence, furnishing fertilizer to Korea...It stretches neither the language nor the purpose of the Act to determine that such sales are not exports."[16]

A similar problem was involved when producers of an anthracite coal used an export association to supply their coal to the United States Army in Germany. Recognizing that a novel issue was involved in a suit under the Sherman Act, the parties to the suit stipulated the facts and agreed to accept the court's decision. Holding that the arrangement violated the Sherman Act, the court enjoined the association from fixing prices, allocating sales, using a common sales agent, and engaging in other activities that might have similar results.[17]

In spite of the exemptions described above, export agreements have had, in practice, surprisingly small effect upon American foreign trade. At the beginning of 1974 there were 32 registered associations with a total of less than 180 members. The number of associations has not been larger than 40 since 1957. Many of the associations, though registered, have been inactive. The Commission's 50-year review of association activity, which is the most recent and also the largest and most detailed source of relevant information, says that the number of active associations, which reached a peak of 42 in the period 1927-1930, ranged between 34 and 25 in the period from 1948 to 1965, and in 1962 was 26.[18] From 1958 to 1962, exports assisted by the registered associations ranged between 2.5 and 2.3 per cent of total United States merchandise exports.[19]

Eighty-five per cent of these assisted exports were concentrated in four product groups in 1962 -- chemicals, food, non-metallic minerals and machinery.[20] For only eight products did assistance by the association account for more than 5 per cent of total exports in 1962.[21] These were: sulphur, 86.1 per cent; motion picture and television film, 80 per cent (estimated; see note 21); carbon black, 69.8 per cent; phosphate, 44.7 per cent; potash, 24.0 per cent; pulp, paper,and paperboard, 14.3 per cent; rice, 13.8 per cent; soybean oil, 8.4 per cent.

With few exceptions, therefore, the Export Trade Act has accomplished little to achieve its purpose. For an industry that consists of small enterprises, the Act has little to offer. Though the firms individually are too small to sell overseas economically or develop new markets there effectively, they nearly always can sell, if they wish, through export merchants or export brokers or to buyers for export. An association could be a source of economy for them only if it could outdo such specialists. There is little incentive for such an industry to try to overcome its inexperience in exporting by using an association.[22] If it makes the attempt, there are two obvious difficulties that tend to increase with growth in the numbers of enterprises involved; first, that the members may be unable to agree about such matters as export quotas, prices and terms of sale in export markets, and whether or not they shall require that all exports be made through the association; secondly, that minorities of the members may find membership burdensome because it involves comformity to rules about such matters that they consider inappropriate to their own interests. Any lack of homogeneity in the products and ways of doing business is likely to add to these difficulties.

For such an industry, the offsetting advantages of being free to undertake concerted restraints in export trade are likely to be illusory. If foreign governments limit competition from abroad, small American exporters, even acting together, can do little to remove the barrier unless aided by pressure from the United States government. Unless the industry's products are homogeneous, their individual appeal in foreign markets that are open to them is more likely to be recognized and preserved by commercial intermediaries that serve export markets than by an association that tries to sell differentiated products at agreed prices and on agreed terms. Unless exports of homogeneous American products are large enough to be a significant part of the supply to export markets, American exporters are likely to encounter in these markets foreign competitors important enough to deprive them of ability to reduce supply there by export quotas, or to set prices there for their exports. To reduce competition among themselves would have negligible effects so long as competition by foreigners remained vigorous.

Considerations such as these were important among the reasons why numerous associations composed of small and medium-sized enterprises never became active, or did so only briefly and were then dissolved. Indeed, in a survey of 80 associations that dissolved between 1918 and 1955,[23] foreign price competition was the reason most frequently given to explain the dissolution. Of the 176 export associations formed in the period 1918-1965, a total of 46 (26.1 per cent) were never active; of the active ones, half were active for short periods not exceeding five years. Only 37 per cent of all the associations, a total of 65, were active for more than five years.[24]

Relatively large enterprises have been conspicuous among the members of export associations and the recipients of export assistance from such associations. The following table for the period 1958-1962 (the period covered by the most recent substantial study of performance under the Act) ranks association members by assets, indicating for each group the percentage of total association assistance in exports received by firms in the group.[25]

Asset Size (Millions)	No. of Members Reporting	Per Cent of Total Members	Cumulative Per Cent of Total	Per Cent of Total Assisted Exports	Cumulative Per Cent of Total
More than $100	114	24.5	-	79.3	-
$50 - $100	38	8.2	32.7	10.6	89.9
$25 - $ 50	37	8.0	40.7	2.5	92.4
$10 - $ 25	56	12.0	52.7	3.9	96.3
$ 5 - $ 10	40	8.6	61.3	1.8	98.1
$ 1 - $ 5	101	21.7	83.0	1.7	99.8
Less than $ 1	79	17.0	100.0	0.2	100.0
TOTALS	465	100.0		100.0	

As this table clearly shows, nearly one third of association members had assets of $50 million or more. These relatively large enterprises made nearly 90 per cent of all exports for which associations provided assistance.

But large enterprises, like small ones, are seldom dependent for export opportunities upon export associations. As small firms can use commercial intermediaries individually, large ones can and do make more exports directly than through associations. In recent years, they have been able to do so more easily because of growing assistance by the Federal government.[26] Operating individually, they can relate their export programs to their programs for foreign investment and expansion in foreign countries without encountering the legal limitations that curb export associations in owning foreign sources of production. Operating individually, they also encounter fewer legal problems in the growing number of foreign countries that have laws to forbid or control restrictive agreements, and incur less risk that their agreements may provoke retaliatory combinations by foreign firms.[27]

Thus for large and small member enterprises alike, though for different reasons, association-assisted exports have been substantially less than half of total exports. In 1962, unassisted exports were only one third of the total exports by members of export associations of the kinds of products covered by those associations, and only one fourth of all exports by those members (including exports of products as to which there was no association assistance).

The record-by-size groups is reported below for 263 reporting firms.[28] The percentages in the last column pertaining to all exports by the members including exports of products for which there was no export association activity.

Asset Size (Millions)	Number of Members	Per Cent of Total Assisted Exports	Per Cent of Total Exports by Association Members	Assisted Exports as Per Cent of Total Exports by Association Members
More than $100	69	80.7	77.1	26.1
$50 - $100	16	9.6	6.2	38.7
$25 - $ 50	18	2.0	6.7	7.5
$10 - $ 25	37	4.9	5.2	23.5
$ 5 - $ 10	21	2.0	2.9	17.3
$ 1 - $ 5	53	0.8	1.8	10.4
Less Than $ 1	49	0.04	0.1	4.1
Totals	263	100.0	100.0	24.9

Large enterprises are likely to obtain advantage from the exemption that lets them collaborate in export restrictions. Being large and few, they usually can manage to agree; and collectively they may be important enough in export trade to affect substantially the foreign markets to which they send their exports. If they were free to make agreements with important foreign producers, they might often become significant parts of a regional or world cartel. Since the 1940's, the government has made it clear that the law does not allow them to do so if thereby the American domestic market or the amount of American exports would be adversely affected. But the law leaves them free to: a) agree with foreign enterprises so far as there can be no such adverse effects; b) dominate foreign markets where their exports are large enough to do so; c) mitigate competition in foreign markets so far as they can do so and are there permitted to do so, by avoiding competition among themselves and thereby reducing the number of competitive options available in those markets. Where such results are achieved, they are likely to

benefit not only the large companies but also the smaller members of the associations involved. The Commission's 50-year review concluded that: "The most active associations have held a dominant position in world markets."[29]

In summary, where American exports are important in world trade and the American industry is an oligopoly, the Act may facilitate the development in foreign markets of oligopoly and in some cases even of monopoly.

This has been a significant aspect of the development of export associations. Large companies have been prominent in most of the associations. Of 42 associations for which the relevant information is available for the years 1938-1962, only five had as members none of the industry's five leading firms. Six of the associations had all five of such firms; ten associations had four of the five; five associations had three of the five; ten associations had two of the five, and six associations had one of the five. The 16 associations that included all or all but one of the five leading firms provided more than 91 per cent of the total association-assisted exports.[30] In 1962, of the total association-assisted exports, 77 per cent came from industries of the kind that have been called Type 1 oligopolies; an additional 15.6 per cent from industries of the kind that have been called Type 11 oligopolies; and only 7.4 per cent from industries less concentrated.[31]

Most export associations have treated restraints in export markets as important parts of their functions. It is difficult to believe that they would have done so if they had thought such restraint devoid of effect upon competition.

In 1962, of the 23 associations for which information about marketing functions is available, 19 were engaged in setting prices and allocating markets, and only the four others regarded as their primary functions such activities as providing information, promoting sales, financing sales, and developing uniform sales contracts.[32]

There has been enduring controversy about the policy of the Export Trade Act. Appraisals that differed widely have been recurrent.[33] The 50-year review that the Commission published in 1967 ended with two recommendations: first, that exemption be given only to firms that can demonstrate need for it; and secondly, that the standard of exemption be so changed that the Commission could reject a registration on the ground that its effect probably would be anticompetitive.[34]

In 1964, as a result of experience in Europe under a research contract for the Department of State, I tried without success to change the focus of discussion of export trade policy from unilateral reconsideration of the policy of the Export Trade Act to multi-lateral consideration of national policies toward export restrictions by private groups. I had found reasons to believe that the governments of Germany and the United Kingdom saw problems in their own national policies towards such arrangements, and that at least the former might be receptive to international discussion of the subject. In my report, I suggested to the Department of State that since each country is likely to incur damage from export cartels of other countries an effort should be made to agree with other countries upon reciprocal reduction of such restrictions, comparable in spirit and technique to the tarriff reductions achieved under the reciprocal trade agreements acts. The Department published my suggestion,

but no action resulted.[35]

In 1967, hearings by an antitrust committee of the Senate focussed upon the Export Trade Act. Conflicting recommendations were made by different government agencies. A spokesman for the Department of Commerce recommended that the exemption be enlarged. The Chairman of the Federal Trade Commission endorsed the proposal previously made in the 1951 report by the Commission's staff, that applicants for exemption be required to show that they needed it. The Assistant Attorney General in charge of the Antitrust Division recommended that the Export Trade Act be repealed because it was seldom used, and then principally for collaboration by powerful firms; had harmful domestic effects upon the industries involved; and set a bad example for other countries.[36] A recommendation for repeal was made again in 1969 in a report by a task force appointed by the President.[37]

In 1972, a bill intended to expand trade included a section that would have empowered the Secretary of Commerce to authorize (subject to disapproval by a majority of the Federal Trade Commission) export programs with "territorial, price maintenance or other restrictions" that might include agreements with foreign competitors, and would have exempted the arrangements from the antitrust laws. In hearings on the bill, the Secretary of Commerce said, "...my own belief is that the antitrust laws need some reconsideration in the light of our international trade problems," and that he meant that the laws should be liberalized in their application to exporters. In the same hearings, the Chairman of the Federal Trade Commission testified against the proposal, and made adverse appraisals of the existing Act. He said, "...in general it has not succeeded in achieving its intended purpose...

Based upon its experience in administering the Webb Act, the Commission has found no empirical evidence that this country's export trade will be faciliated by the sort of concerted activities which could be authorized under Title V11 -- including price fixing, territorial restrictions, and resource pooling...In situations where Webb associations have reported that they have not been successful in expanding exports, the reasons given have not been that the Webb antitrust exemption is too narrow...The History of the Webb-Pomerene Act also indicates that export trade associations may be convenient vehicles for American corporations to reduce competition in domestic markets and to cooperate with foreign cartels in controlling world prices and markets...our experience tends to show that cooperative activity among typical export association members, which are large firms operating in domestically concentrated markets, is likely to have adverse effects on competition in the domestic market..."

When asked if he would suggest that the Act be repealed, however, he replied, "No, sir; I would not. I think that the striking thing about the Webb Act is how little help it has been. Any help at all, as I said, 2 per cent of the foreign commerce of this country, is Webb assisted, and it does no damage to our country. I would not want to take away that assistance."[38]

Though the implications for antitrust policy of the growth of multinational corporations have become matters of growing concern in the United States, the relevance of this growth to the policy of the Export Trade Act has not yet received official attention, so far as I have been able to discover. Thus far, though large companies simultaneously enjoy the benefits of the Act's exemptions and also make substantial exports individually, those who make and apply

export trade policy have not explored the impact of the exempt collective action upon the individual exporting policies of the large member companies. Though the growth of the multinationals probably enlarges and complicates any problems that such relationships create, it is not surprising that, so long as the existing problem receives no attention, the emerging large one is also ignored.

111. EXPORT AGREEMENTS

Footnotes

1. Federal Trade Commission, Economic Report, Webb-Pomerene Associations: A 50-Year Review, Staff Report to the Commission, June 1967 (hereafter called Review), pp. 1-8.

2. The full text of the Act appears in ibid, pp. 73-75.

3. Ibid, pp. 15, 76.

4. The text of the "silver letter" appears in ibid, pp. 102-106.

5. United States Alkali Export Association, v.U.S., 325 U.S. 196 (1945).

6. U.S.v. United States Alkali Export Association, 86 F. Supp. 59 (S.D.N.Y. 1949).

7. Civil 33-275, Southern District of New York (1945, amended 1947).

8. U.S.v. Minnesota Miningand Manufacturing Co. 92 F. Supp. 947 (D. Mass. 1950).

9. Review, op. cit., note 1, p. 109.

10. Review, op. cit., note 1, p. 110.

11. Federal Trade Commission, reports on International Phosphate Cartels (1946), The Copper Industry (1947), The Sulphur Industry and International Cartels (1947), International Steel Cartels (1948), International Electric Equipment Cartels (1948), The Fertilizer Industry (1950). The last report set forth the connection between the export association

for potash and the European potash cartel, and noted (page 123) that since the European cartel had disappeared during the war there was no good reason to recommend adjustment of the export association's connection with it.

12. Review, op. cit.,note 1, pp. 106-107.

13. Ibid, pp. 107-108

14. In the light of the prohibitions numbered 5 and 8 in the list that ensues, the Commission's view apparently is that prohibitions of withdrawal and of subsequent competition with the association are permitted if reasonable in duration and non-discriminatory, but not otherwise.

15. This permission apparently is limited by the prohibitions set forth under the numbers 3C, 4, 7, and 9. The apparent intent is to permit agreements with foreigners by which foreign markets are divided, but only if they do not involve, either directly or indirectly, reducing the amount of American exports or restricting American imports.

16. U.S. v. Concentrated Phospate Export Association, Inc., et al., 393 U.S. 199 (1968).

17. U.S. v. Anthracite Export Association, et al., 1970 Trade Cases #73,348. Where American aid programs are involved, it is possible that the Sherman Act reaches even further. In a recent private suite in which the problem centred upon the relationship of that Act to the requirements that American ships be used in carrying aided goods and to exemptions contained in the shipping legislation, a court decided that the Sherman Act applies to concerted efforts to drive certain American firms out of the business of

carrying products between foreign ports. "We hold that plaintiffs were engaged in the foreign commerce of the United States for purposes not only of determining constitutional power, but also of determining the applicability of the Sherman Act." As to arguments that the restraints were exempt under the Shipping Act, the court ruled that such exemptions must be narrowly construed. "We are not to turn to the acts of subsequent Congresses for unstated exemptions or implied repeals of the anti-trust laws." The Supreme Court refused to grant a writ of certiorari. See Pacific Seafarers, Inc., *et al.*, v. Pacific Far East Lines, Inc., *et al.*, 404 F. 2d 804 (D.C. circuit 1968); cert. denied, 393 U.S. 1093 (1969).

18. Review, *op. cit.*, note 1, p. 87.

19. *Ibid*, p. 36. The period is one for which the Commission studied all registered associations and their members. Its review, published in 1967, provides the most recent reliable information. It notes that figures from registered associations had overstated the amount of assistance by including unassisted exports by member companies. For the years 1960-1962, for example, the percentages reported by the associations included unassisted exports about as large as assisted exports (*ibid*, pp. 23-24, 35-36, and 112-113). Even including members' unassisted exports, however, the total did not exceed five per cent during the period.

Only totals thus exaggerated are available for other periods. These appear to indicate, however, that results for 1958-1962 fairly represent those for the entire history of the Act. Percentages somewhat higher were attained in the late 1920's and early 1930's

-- including the exaggerations, an average of 12.2 per cent for the period 1930-1934, averages of 7.9 per cent for 1925-1929 and 6.2 per cent for 1935-1939. Somewhat lower percentages (2.1 per cent) existed in the war period, 1940-1944. (Ibid, p. 23).

20. Ibid, p. 33.

21. Ibid, pp. 41 and 53. Census data on motion picture exports are compiled on the basis of production cost, not revenue. Hence the percentage for them is not comparable with those for the other products. The recorded percentage was estimated.

22. Cf. Ibid, pp. 61-64.

23. Ibid, p. 27. The survey covered reasons for dissolving 80 associations, between 1918 and 1955. The reasons most frequently given were foreign price competition (35 associations) and government restrictions of trade such as tariffs, quotas, and licenses (17 associations). Some of the other reasons, as stated, may or may not have reflected the pressure of foreign competitors: e.g., "ceased conforming to the Webb Act" (11 associations), "members decided to export individually" (6 associations) and "resources depleted" (3 associations).

24. Ibid, p. 26.

25. Ibid, p. 44.

26. Cf. Ibid, p. 64.

27. Some foreign laws, that of West Germany for example, apply broadly enough to restrictive agreements that they probably cover restrictions by American export associations.

Indeed, the German law explicitly applies to restraints that have effects in Germany, even though they result from acts done elsewhere (Section 98 (2)). Similarly, some foreign laws permit combinations against foreign restrictions. The German law authorizes a cartel authority to approve a defensive agreement by importers when there is no competition or only insignificant competition among suppliers (Section 7). In the United Kingdom, the Restrictive Practices Court found the existence of a sulphur buying group to be justified under a provision of the British law as a means to counteract the activities of the American sulphur export association. (In re National Sulphuric Acid Association Agreement, 4 R.P. 169 (1963)).

Such problems have become more likely as the number of relevant foreign laws has increased. By 1969, such laws existed in 24 foreign countries. See Corwin D. Edwards "The World of Antitrust," Columbia Journal of World Business, July-August 1969. For more detail, see Corwin D. Edwards, Control of Cartels and Monopolies, an International Comparison, Dobbs Ferry, N.Y., Oceana Publications, 1967, pp. 337-369.

28. Review, op. cit., note 1, pp. 63-64.

29. Ibid, p. 51.

30. Ibid, p. 47.

31. Ibid, p. 46. The classification of oligopolies was applied by Carl Kaysen and Donald F. Turner in Antitrust Policy, Cambridge: Harvard University Press, 1959, p. 30. Type 1 consists of industries in which the largest eight firms provide 50 per cent or more of domestic shipments and the largest 20 provide 75 per cent or more. Type 11 consists of

industries in which the largest eight provide more than 33 per cent but less than 50 per cent, and the largest 20 provide less than 75 per cent.

32. Review, op. cit., note 1, pp. 48-50.

33. Appraisals prior to 1967 have been summarized in Ibid, pp. 8-14.

34. Ibid, p. 70. The second recommendation was stated less explicitly. It says, "...it would appear justified that probable domestic effects on competition be more specifically considered as a matter determining the acceptability of any registration request."

35. My reasons for making the suggestion were summarized in a letter that I wrote several years later, which appears at pp. 867-869 of Export Expansion Act of 1971, Hearings before the Subcommittee on Foreign Commerce and Tourism of the Senate Committee on Commerce, 92d Congress, 2d Session (1972). The suggestion appears in Corwin D. Edwards, Cartelization in Western Europe, Policy Research Study, Bureau of Intelligence and Research, Department of State, June 1964, pp. 92-94.

36. See International Aspects of Antitrust, Hearings before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 90th Congress, 1st Session (1967). The recommendations from the Department of Commerce appear at pages 179-180; that from the Chairman of the Federal Trade Commission at page 139; that from the Assistant Attorney General at page 125.

37. White House Task Force Report on Productivity and Competition, (the Stigler Report), 115 Congressional Record 647 (daily edition, June 16, 1969).

38. Export Expansion Act of 1971, op. cit., note 35. The bill, S1754, appears on pp. 3-47; the statement by the Secretary of Commerce on p. 68; the statement quoted from the testimony by the Chairman of the Federal Trade Commission on pp. 233-235 and 242.

1V - SYSTEMATIC DELIVERED PRICING

Delivered price formulas have been subject to American antitrust law in two respects: first, as means for restrictive agreements, and secondly, as formulas that may include discriminations in price. Cases involving them sometimes have concerned the first aspect only, sometimes both aspects, and sometimes the second aspect only.

What follows will focus upon the relevance of such pricing formulas to restrictive agreements. Their discriminatory aspects will be included in the discussion of price discrimination.

There are several types of delivered price systems which, for clarity, must be discussed separately. In 1959, I described them as follows:[1]

> ...the term uniform delivered pricing means charging the same delivered price at all destinations; the term zone pricing includes all those systems the effect of which is to establish two or more territorial zones between which delivered prices are different and within any one of which delivered prices at all destinations are identical; a single basing point system is one in which delivered prices are computed as though goods originated at a single point of origin, and consist of the price at that point plus freight from that point to the destination; a multiple basing point system is one in which delivered prices are computed as though goods originated at two or more points of origin, but with some points of production not treated as basing points; and a freight-equalization is like a multiple basing point system except that all points of production are basing points.

In multiple basing point and freight-equalization systems, the basing point used in computing a delivered price at a given destination is the one which results in the lowest delivered price; and all sellers quote that price even if, in doing so, they fail to cover all of their actual delivery expense. Such failure is described as absorbing freight. In basing-point systems, single and multiple, shipments from points of production that are not treated as basing points may result, particularly at nearby destinations, in expenditures for freight that are less than the computed freight charges from the applicable basing point. The excess of the transportation charge collected from the buyer over the transportation expense actually incurred is described as phantom freight. (The term phantom freight is also applied to excess charges due to use of a more expensive method of transportation in computing freight than in shipping the goods.) In basing point systems, computed freight costs are greater than actual freight expenditures at some destinations, less at others; that is, there is both phantom freight and freight absorption. In a freight-equalization system, there is freight absorption, but no phantom freight.

Proceedings about use of delivered price formulas in price agreements have been simplified by the fact that price agreements are unlawful per se under either Section 1 of the Sherman Act or Section 5 of the Federal Trade Commission Act. A delivered price system is clearly unlawful if it is so used that price fixing results; and analysis of such a system can centre upon the question whether or not this is so. Such analyses differ in complexity for different kinds of delivered price systems.

Uniform Delivered Pricing

Some products that are sold throughout the United States are sold by each maker at a price that is uniform for all delivery points. This is true, for example, of various periodical publications. But the national uniformity of each maker's delivered prices is not indication that there is price agreement among makers of rival publications. Indeed, different national prices for such publications may express quite different price policies by the rival makers. The absence of territorial differences in the delivered prices may mean only that the location of delivery has such small effects upon cost of transportation, as has been the case for periodicals delivered by mail, that the convenience to each seller of quoting only a single delivered price outweighs the costs of doing so. Such a single price, for example, may simplify advertising and selling and facilitate retention of the subscriptions of those buyers who move to new localities.

The question whether or not the national delivered prices of rival sellers constitute a price agreement is like the question whether or not rivals who sell only in a single locality have agreed upon prices; in both of these situations, the mere territorial scope of the price quotation contributes little or nothing to the answer. The key issues are whether or not the delivered prices of the different sellers who supposedly compete are enduringly and reliably identical or enduringly and reliably show stable and continuing relationships; and if so, what is the explanation for these results.

Thus, where there is uniform delivered pricing, that fact contributes little or nothing to the existence of a price agreement

nor to proof that such an agreement exists. Few legal proceedings are focussed upon such agreements. During the 20 years when the significance of price fixing by delivered price formulas was being most actively explored, six instances of uniform delivered pricing (among 46 against delivered price agreements of all kinds) resulted in orders by the Federal Trade Commission.[2] In these cases evidence of agreement did not rest significantly upon the delivered pricing formula. The antitrust agencies developed no clear theory of connection of the formula to price fixing, and no controversy arose about any such theory.

Zone Pricing

When delivered prices, instead of being nationally uniform, are set at different levels in two or more zones, price agreements usually are more easily perceived and usually are vulnerable to legal attack focussed upon the delivered pricing systems. For zone prices to be agreed prices, sellers must maintain, in spite of their different locations, pricing zones that have identical boundaries. Within each zone, sellers ignore differences in the location of buyers, even though in selling they may incur substantial differences in transportation expense. At the boundaries of zones, however, small differences in the location of buyers, trivial as to differences in transportation cost, become the reasons for appreciable differences in delivered prices, the amount of these differences being the same for all sellers who offer to sell at these locations, whether or not they themselves are located near to or far from the boundaries. For sellers differently located to concur in such pricing is not easy. Therefore, the negotiation by which the zones were agreed upon is likely to have left a trail that can be discovered by investigation. At the zone boundaries, moreover, buyers who pay higher prices than nearby buyers

are likely to complain and thus bring the artificiality of the zonal system to the attention of the antitrust authorities. When a system of zone prices is scrutinized closely, the territorial boundaries of the zones are likely to be obviously artificial in the sense that the territorial price differences are clearly inappropriate to competition for sales by at least some of the sellers who adhere to these differences. Thus zonal delivered prices are peculiarly vulnerable to antitrust attack.

In the period 1936-1955, the Federal Trade Commission issued 26 orders in price fixing cases that involved zone pricing. In 23 of these, zone delivered prices are not complicated by other formulas, in two, basing point pricing was also involved, and in one, also freight-equalization.[3] Nine of the decisions were appealed. Decisions by the appellate courts affirmed the Commission's order in four cases, affirmed it with modifications in four more, and set it aside in one. Only one of the cases reached the Supreme Court, and in this the only issue decided by the court was whether or not the Commission had power in a conspiracy case to issue orders about the conduct of the companies acting individually.

This case well illustrates the nature of the legal proceedings involved.[4] National Lead and others were using a system of zones that differed by product classes and quantities. The most eleborate of these zones divided the country into seven zones for a given class of products, with a differences of $1 per 100 pounds between the highest and lowest zone prices. For a second class of products, the country was divided into two zones for carload shipments and four zones for smaller shipments, with a range of 75 cents between the highest and lowest zone prices for the smaller shipments. For a third class of products, two zones were used for all sales, with a price difference of 25 cents

between zones.

The Federal Trade Commission order forbade the companies to agree to maintain zone prices or use any other system that resulted in identical price quotations. It also forbade the companies individually to sell at zone prices for the purpose or with the effect of systematically matching delivered prices. This part of the order was explained in the opinion as necessary to effectiveness in eliminating conspiracy, since without it "the momentum of the system, so firmly and maturely established, might last for some time."[5] On appeal, the circuit court affirmed the Commission's order except as to the part of it that forbade zone pricing by individual sellers. This part was set aside as inappropriate to a conspiracy case. Review by the Supreme Court covered only the propriety of the order against individual conduct in matching delivered prices. The Supreme Court sustained the order.[6]

The issue decided by the Supreme Court was of major importance. The Commission's power under the Federal Trade Commission Act is to order violators of law to "cease and desist" from their violations. In a conspiracy case, this obviously justifies an order to cease agreeing. It is not obvious, however, that in such a case the Commission can order individual parties to the agreement to refrain from doing things that, if done individually without conspiracy, would not be violations of law. It is still less obvious that the power to order that particular conduct to cease can be stretched to include power to direct that particular acts be done. This was the kind of problem that was decided by the Supreme Court in the National Lead case.

If, after a delivered pricing formula is well established, the parties to it are told

merely to cease agreeing that they will use it, there is possibility that each of them might decide individually not to change a pricing method that had served well. Thus the various prices of the various companies might continue to mesh with one another as before, with continuance of the former identities in the delivered prices. This would be the so-called "momentum effect". Precautions against it would be orders to some or all of the parties to the conspiracy to change their prices or pricing methods sufficiently that continuance of price relationships similar to those of the old conspiracy would necessitate a new agreement. It is immaterial whether such an order takes the form of a requirement that specified changes be made or, as in the National Lead case, of a prohibition that former practices and purposes be continued by individual action. Either kind of order can serve the corrective purpose, and little ingenuity is required to convert an order from one mandatory in form to one prohibitory in form, or vice versa.

Basing-Point Systems

The kind of delivered pricing that is most flexible, least visibly restrictive, most complex, and most difficult to attack legally is the basing-point system. Such systems have been the other principal target of proceedings against price fixing by use of delivered price formulas. Though formulas with single basing points and formulas with several such points differ in important respects, these differences are important chiefly as to problems that arise under the law of price discrimination. In cases that focus upon price agreement, the differences between the two types of formula consist primarily in the magnitude of certain anomalous price relationships that, except as to magnitude, are common to both types. Hence both types will be discussed here

together.

In a basing-point system, a producer establishes a price at some location, almost always the location of his plant, and sells at delivered prices that consist of the price at the plant plus transportation charges to the destination of each shipment. The prices of that producer are prices f.o.b. plant. Each of the other producers decides individually whether or not to establish a similar price at his own plant. If none does so, the result is a single basing-point system; if one or more of them also sets a plant price, but some of them do not do so, the result is a multiple basing-point system. In both types of system, some points of production do not have individually established plant prices. The peculiar feature of both systems consists in the relationships of the prices of sales from plants not located at basing points to those of plants that are located at such points.

In a single basing-point system, the producer at the basing-point sets the price there and then quotes delivered prices derived from it elsewhere. Each producer not located at the basing point adopts these delivered prices. As the industry describes the system, the non-basing-point producers meet delivered price competition by selling at the same delivered prices. The basing-point producer is the price leader; only he institutes any price change, upward or downward. The changes may be due either to a change in the basing-point producer's plant price, which automatically results in corollary changes in his delivered prices, or to change in transportation costs from the base to some or all destinations, which the basing-point producer then incorporates in his delivered prices. In either case, each such change promptly results in identical changes in the delivered prices of all the other producers. The result is as though all producers were

located at the basing point, adopted plant prices identical to those of the basing-point producer, and then added transportation costs from the base to each destination.

In a multiple basing-point system, there are two or more basing points, each with a basing-point producer who has a base price from which destination prices are computed by adding transportation costs. At destinations near a base, the price at that base plus transportation costs from it results in delivered prices lower than those that would result from computations consisting of plant prices at any other base plus transportation costs to the destination from that other base. The delivered price that is recognized as appropriate for any destination is the lowest of the different delivered prices that such computations could make applicable there; and all destinations that are thus attributable to the plant price at one base are recognized as part of the area of that base. Thus each plant at a basing point acquires an area within which its plant price determines delivered prices. If one basing-point producer sells at a destination that lies within the area of another basing point, he does so, not at a delivered price computed from his own base, but at the one computed from the other base and thus the one lowest for that destination. Thereby each basing-point producer is the recognized price leader in its own basing-point area, and price leadership is, in effect, allocated territorially among producers located at basing points.

Any one of these producers, however, can by his own decision enlarge or reduce the area of his territorial leadership. If he raises his plant price, he increases his delivered prices and thus, at the boundaries of his basing-point area, loses control of certain

destination prices that now are lower if computed from another base at which plant prices have not been increased. Conversely, if plant prices at one base are reduced, delivered prices computed from that base become lower than before, and thus lower at some destinations at the boundary of the basing-point area than destination prices computed from a different base that formerly set the delivered prices there. Thus, by changes in their relative plant prices, basing-point producers can enlarge or reduce their basing-point areas. In effect, the basing-point producers compete in prices, but only at the boundaries of basing-point areas. The price leadership of each of them as to most of his business remains undisturbed. Wherever the destination price of each constitutes the lowest delivered price, other basing-point producers who sell there accept the leadership.

The prices of producers who are not located at basing points fit into such a system without difficulty. In selling at any destination, including his own plant, such a producer adopts the delivered price that the basing-point producer has established there. Within the area of the basing point in which the non-basing-point producer is located, that producer follows the lead of the plant at the basing-point. Within any other basing point area, he follows the lead of the basing-point producer who sets the price there. He is consistently a follower, though at different destinations the leaders differ.

So long as the basing-point formula is followed, delivered prices at all destinations are identical for all producers both in single basing-point systems and in multiple basing-point systems. Each producer knows that this will continue to be so. None need anticipate price reduction by another except in the ways that the formula recognizes; a) reductions in delivered

prices that reflect reductions of plant prices by a producer at a basing-point; b) reductions in delivered prices that reflect reductions of transportation costs from the base to the destination. Though every non-base producer is free to establish an additional basing point, this happens rarely; and if it does, the perturbations incident to readjustment soon become merely somewhat more complex applications of a familiar multiple basing-point formula to a system with an additional base. The formula results in prices so reliable that they seldom fail to be quoted even when large attractive orders are offered to the producers under sealed bidding requirements. In the language of the Federal Trade Commission, the prices are consistently "matched."

The foregoing analysis pertains to fully developed basing-point systems, of the kind that have been condemned as price fixing. Some delivered price systems of the basing-point type stop short of this full development. In one instance, for example, though there were non-base plants that consistently quoted destination prices computed as though these plants were located at the base, those plants did not consistently follow the lead of the producer at the base, but repeatedly initiated their own changes in base prices. After investigating this situation, the Federal Trade Commission did not file a complaint.[7]

Application of the law to basing-point systems has involved difficulty for several reasons. Some of the most conspicuous instances of such formulas had existed for several decades, so that, if they had been established by negotiation that expressed anticompetitive purposes, this fact was neither recent nor clear, and whether or not the original purpose still guided current activity was also uncertain. In two early cases that involved charges of

price fixing by industries that used basing-point systems, the proceedings had focussed upon other aspects of conduct, and the government had lost the cases.[8] Though zone pricing had been successfully attacked in another case and use of a basing-point system in still another, in neither of these cases had the delivered pricing system been central as the price-fixing method.[9] Thus the legal status of pricing formulas was uncertain.

Moreover, basing-point systems had developed sometimes in ways that did not appear to be conspiratorial. In the steel industry, for example, early producers were located in or near Pittsburgh, so that sale by them at Pittsburgh prices plus freight from Pittsburgh to the destination of the shipment supported no inference that the pricing formula was the result of conspiracy. When prices were quoted f.o.b. Pittsburgh, these prices were lowest in Pittsburgh and higher elsewhere by the amount of the freight from Pittsburgh, which for steel was substantial. Producers of steel had incentives to establish their new capacity in places far from Pittsburgh that consumed substantial amounts of steel, since by doing so they could add to their plant prices roughly the amounts that companies located in Pittsburgh would need to expend in freight charges to reach these distant places. Increasing portions of total producing capacity were located near places like Chicago. Sale at Pittsburgh prices plus freight from Pittsburgh became decreasingly appropriate to the current facts as to location of sellers. What had originated as sale f.o.b. plant had evolved into use of a basing-point system with a single base at Pittsburgh.

But in such cases, and notably in the case of steel, such results were not clearly attributable to agreement upon a pricing formula. The largest producer was likely to be the first to establish

important plants far from the basing point, as was United States Steel at Gary, Indiana, near Chicago. Smaller companies that sold at the same prices were following the price leader and getting prices as high as they could, but in doing so they were not necessarily conspiring with United States Steel. Under such circumstances, if the system was subject to legal challenge, it could be interpreted, as it actually was in the steel industry, as unconscionable conduct by a powerful company, and a proceeding against that company could be thought both appropriate and adequate to provide a remedy. Accordingly, when the Pittsburgh-plus system was attacked by the Federal Trade Commission, attention was focussed upon the distortion of business opportunity that resulted from the system's phantom freight. The proceeding was focussed upon United States Steel only, and the order was concerned only with that company's conduct.[10]

Between the steel decision in 1924 and 1943, when the Federal Trade Commission issued an order against the multiple basing-point system in the cement industry, the conception of the operation of basing-point systems with which this part of this paper began was developed not in legal proceedings but in official reports and the writings of private scholars. Reports analyzed the operation of the system in the cement industry and the steel industry, an important multi-agency governmental committee recommended that legislation make such systems illegal, and hearings were held upon a bill designed to do this.[11]

When the Commission decided in the mid 1930's to take legal action against basing-point systems as conspiracies, it had difficult problems of proof. Producers located at basing points in a multiple basing-point system did not necessarily quote identical prices at their respective plants

nor change their plant prices at the same time, or even in the same direction. What the Commission saw as matched prices derived from collusion could be described instead as competition in which each seller met the prices that he found in various territorial markets. An anomalous characteristic of single basing-point systems--the fact that non-base producers usually received at their own plants and at nearby destinations prices that included substantial amounts of phantom freight--made these destination prices look unreasonable; but in multiple basing-point systems (which were becoming more important as new basing points appeared in industries in which originally there was only one) the larger number of basing-points reduced the size of the phantom freight charges and made the system look less anomalous. Moreover, what looked highly artificial when it took the form of pricing based upon a point far from the point of production could be so described that it sounded more natural -- for example, as a plant price at the level of the former delivered price as computed from the base (including all the phantom freight received there), with delivered prices reduced elsewhere by enough freight absorption to avoid being outsold at these other destinations by the producer located at the base. Where basing points developed gradually, like the one that existed in the latter part of the 1930's in the steel industry, and were applied by accretion of custom as well as by agreement, the result could look to the casual observer like competition modified by price leadership.

Evidence that basing-point systems were due to agreement rather than to competition was obtained most easily from two aspects of such systems: first, efforts to perfect the formula by eliminating minor deviations in the way that it was applied; and secondly, efforts by the industry to discipline those of its members who refused to use the formula or surreptitiously did not follow it.

Attempts to perfect the basing-point formula differed in particulars from industry to industry. Among the most striking manifestations were these:

1. Even with the incentive of unusually large orders to be awarded by sealed bidding, and under conditions in which there was much idle capacity and much disagreement about the probable trend of demand, non-base plants refrained from initiating price reductions, and base plants selling outside their own base areas refrained from reducing prices there by absorbing more freight than would meet the destination prices appropriate to the delivered prices of the base mills that were recognized as leaders at the destinations.

2. To assure that freight charges made by all sellers were the same from each applicable base to each destination, basing-point industries usually compiled these charges in freight-rate books issued by the industry, instead of letting each producer find them among rates published by transportation companies. To avoid differences in the speed with which changes in transportation costs were used in computing delivered prices, some industries applied the changed rate, not when it went into effect, but at a later date when the industry recognized it as applicable.

3. Where particular transportation rates, such as those for shipment by water, were uncertain, or differed from different carriers, or changed frequently, the industry sometimes computed and used charges by rail only, even if the shipment was actually made by some other type of transport.

4. Where some members of the industry could deliver by water while others could not, industries often applied rail costs, used by the members that shipped by water as well as by the others. Some-

times, where water shipment rates were used under such circumstances, this was done only after those who could not ship by water expressed willingness to adopt the same rates.

5. One industry, concerned about tiny differences in delivered prices that sometimes appeared when different sellers used different railroads in computing transportation costs to the same destination, even tried to get the railway association to adopt a uniform rule about the treatment of fractions of a cent in freight charges. It complained that when there were such fractions some railroads conceded the fraction to the shipper, some added enough to complete the full cent, and some made either concession or addition, depending upon whether the fraction was less or more than half a cent; and that in consequence the formula did not reliably result in identical transportation costs from the base to the destination.

6. To prevent buyers from paying less than the delivered prices appropriate to their locations, producers usually refused to make sales to them for delivery anywhere else. In some industries, in which the buyers shipped their own products in their own trucks, these trucks sometimes discharged their loads near the plant of one of the industry's producers and sought to reduce costs by buying at the plant and carrying the product home in the empty truck; but the plant either refused to make such sales or made them only at the delivered price appropriate to the buyer's location.

7. In at least one industry (cement), though some buyers found differences in the products of different suppliers that were so important to them that they applied their own tests of quality, the producers of the superior products did not proclaim, or even acknowledge, the differences, but agreed with the rest of the industry that the products of all producers

were uniform.

8. In some industries powerful buyers -- e.g., automobile companies buying sheet steel for delivery at Detroit -- were able to obtain discriminatory price concessions for delivery at their particular destinations. Such anomalous departures from the formula were adopted by all sellers, with precise and uniform definition of the amount of the concession and of the territory to which it applied.

9. From time to time, a member of an industry became aware of a delivered price, quoted or charged by another member at a particular destination, which seemed to him to differ from the appropriate price under the basing-point formula. Such instances frequently led to inquiries that asked the price maker to explain the price; the usual reply to such an inquiry was either an apology for an error in pricing, with assurance that it would not recur, or else an explanation defending the price as a correct use of the formula.

Instances of disciplinary action also appeared from time to time in basing-point industries, their targets being firms that flouted, sabotaged, or surreptitiously evaded the formula. The most frequent one was establishment of a so-called punitive base, that is, a basing point established, at or near the plant of the producer to be disciplined, by some producer not located at that point. Such a base was used by the company that established it, and also by the others, as one at which to quote an unusually low base price. Since a large part of the recalcitrant producer's sales was likely to be made near his plant, the low base price became means of reducing prices where he was most hurt by the reduction without reducing prices in the other basing-point areas, and hence with

only boundary-line effects upon sales in those areas by the companies that applied the discipline. Even in selling in parts of the area of the disciplinary base at delivered prices computed from the disciplinary base price, the losses of those that applied the discipline were mitigated by the fact that their actual transportation costs to these destinations might be lower than the costs imputed though not paid by them to the destinations from the disciplinary base. Under such selective price pressure, recalcitrants often mended their ways, after which use of the disciplinary base was terminated.

Other means of discipline were also sometimes used. In the cement industry, there were boycotts of dealers who sold foreign cement, which was not received by them from sellers who used the basing-point formula.

Characteristics of basing-point systems like those just summarized led me to say publicly in 1949 (while I was the Commission's chief economist) that "...there is a clear distinction between competition and conspiracy in the way businessmen think and act and in the way prices behave...If there is a member of an industry who has accepted its trade practices without bothering about their effect on competition, a few minutes of self-analysis should be sufficient to enable him to be sure of what he is doing. Such persons must be rare; and there cannot be such a thing as an industry-wide conspiracy of which all the participants are innocently unaware."[12]

Legal action by the Commission against basing-point systems as price-fixing agreements resulted in 11 orders between 1938 and 1955. In two of the cases the facts were complicated by zone pricing also, and in one by industry rules about freight allowances. In the other

eight cases the basing-point formula was the sole target of the conspiracy charge. Only two of the cases were complicated by problems as to price discrimination. Five of the orders were appealed. In the circuit courts four were affirmed and one was set aside. Two of these cases reached the Supreme Court, where the orders were affirmed; and as to a third, the Court denied certiorari.[13]

The cement case, the first in which the Supreme Court decided the status of basing-point systems as instruments of conspiracy, became a test case for the Commission's theory of the applicability of the law to such systems.[14] Though this case included a charge of price discrimination, this charge rested upon the discriminatory effect of agreement to use a system that was inherently discriminatory, so that in analysis and decision the two charges were a coherent whole. The opinion sustained and enforced the Commission's order. It found that the industry's multiple basing-point system had made the prices of all producers identical at all delivery points, in sealed bids as well as in open sales, and that preservation of these identities had been undertaken by numerous activities, including boycott of dealers who sold foreign cement, pledges not to sell at mill prices to buyers who brought their own trucks to the mills, preparation and use of freight-rate books that assured identity in computing transportation costs, and disciplinary action against producers who disregarded the formula, in the form of quotation of reduced prices from "punitive bases" established near the plants of these recalcitrant producers. Reviewing arguments by economic witnesses for the industry, to the effect that competition could produce a multiple basing-point system in an industry such as

cement, in which a standardized product incurred relatively high freight costs, the opinion held that the Commission was justified in concluding that such influences could not account for "the almost perfect identity in prices, discounts, and cement containers."

Moreover, in discussing the charge of price discrimination, the Court summarized its two previous decisions (each concerned with price discrimination by a single company) by saying that their combined effect "was to forbid the adoption for sales purposes of any basing-point system."

In the early proceedings against basing-point conspiracies, the Commission was concerned lest its orders that the parties stop agreeing to use the formula might be inadequate because of "momentum effects" similar to those discussed above as to zone pricing. Until the National Lead decision by the Supreme Court in 1957, the Commission was uncertain whether or not, in a conspiracy case, it could order individual companies to cease using pricing systems that were not illegal unless used by agreement. Thus it was not sure that it could order them individually to abandon the pricing formula. Without such orders, it feared, each company might continue to use the formula, abandoning only some of the concerted conduct by which the system had been perfected, and there would be difficulty in proving that the continuance was collusive, not individual. A momentum effect was thought to be a substantial danger.

In a case against a basing-point conspiracy as to rigid steel conduit, the Commission provided a basis for orders against participants individually by dividing the charge into two counts. After charging conspiracy in the first count, it also charged in a second count that each seller, individually, had violated the

Federal Trade Commission Act by using a basing-point system concurrently with the others. The ensuing order not only directed the participants to stop agreeing but also directed each of them to cease using a basing-point system or selling at prices that systematically reflected "the inclusion of a transportation factor greater or less than the actual cost of transportation" for the purpose or with the effect of "systematically matching delivered price quotations with other of said respondents or producing the equivalent of such matched delivered prices through discrimination in the mill nets received."[15]

The order was sustained by the appellate court, which said: "Each conduit seller knows that each of the other sellers is using the basing-point formula; each knows that by using it he will be able to quote identical delivered prices and thus present a condition of matched prices under which purchasers are isolated and deprived of choice among sellers so far as price advantage is concerned. Each seller must systematically increase or decrease his mill net price for customers at numerous locations in order to match the delivered prices of his competitors. Each seller consciously intends not to attempt the exclusion of any competition from his natural freight advantage territory by reducing the price, and in effect invites the others to share the available business at matched prices in his natural market in return for a reciprocal invitation."[16]

The Supreme Court divided four to four, with the result that the order by the appellate court became final without further clarification of the legal issues involved in the case.[17] The immediate importance of the type of order issued under the second count of the conduit case was removed, however, when in the National Lead case the Supreme Court affirmed the

validity of orders against individual companies in conspiracy cases.

Freight Equalization

The culmination of increase in the number of bases in a basing-point system is a system in which every plant has a plant price and sells at all destinations at delivered prices that consist of that price plus transportation cost from the plant. Under such a system, phantom freight disappears, and the delivered prices become the equivalent of prices from sales f.o.b. plant. In such a system, where the seller encounters a lower delivered price derived from transportation from some other plant, he sells at that price. Thus there is systematic absorption of freight by which all delivered prices at all destinations are identical from all sellers. As in a multiple basing-point system, each seller is free to set his own plant price at whatever level he chooses; the plant prices at different plants may differ and may change at different times; and the effects of changes in a plant price, relative to prices at other plants, are to alter the boundaries of the area beyond which the seller can conform to the formula only by absorbing freight and to alter the amounts of his freight absorption at destinations beyond those boundaries. If every seller uses the formula and adheres to it precisely, such a system of freight-equalization can be used, like a basing-point system, as a means by which delivered prices are kept identical and each participant becomes price leader in an area well defined by the formula itself.[18]

In the period 1936-1955, the Commission issued five orders against freight-equalization conspiracies, and two more orders in cases in which freight equalization was associated with other pricing formulas. In two out of the five

that involved only freight equalization, the order was appealed. In one of these it was modified and affirmed; in the other, modified and enforced.[19] The cases involved no matters relevant to conspiracy by formula that need discussion here.

The cement decision resulted in a major effort by various industries to amend the laws applicable to formula pricing conspiracies and to price discrimination.[20] A guiding memorandum designed to frame the issues for those who sought amendment said in part "...that delivered pricing does not and cannot, of itself, result in price fixing; that price competition can and does exist under delivered pricing methods; that under straight f.o.b. mill pricing there would be less, not more, price competition than under delivered pricing methods because the latter enable more sellers to compete in more markets, while the former restrict each seller to a narrow market..." Recognizing that there was no possibility of legalizing phantom freight, single basing-point systems, and some zone pricing systems, the brief expressed hope that two types of delivered pricing could be made lawful, the multiple basing-point system where every factory sells f.o.b. mill, absorbing freight where necessary to meet competition in other mills' territories, and "the universal delivered price method." It hoped also to legalize "such variants of the above methods as the maximum freight allowance (e.g., buyer's actual freight allowed up to 30 cents per hundredweight."[21]

After much controversy, a bill with provisions subject to conflicting interpretations was passed by both houses of Congress, but vetoed by the President in a statement that said it would obscure the law and weaken antitrust protection. The Congressional majorities

had been too small to override the veto, and subsequent efforts to amend died in Congress. The controversy is significant here only because it produced some further interpretations of the law by the Commission and because it apparently affected the direction and vigor of later enforcement.

Because the controversy pertained to proposed changes in the law, the Commission found it necessary to consider the concepts of the recent decisions not only in their application to the cases that had been decided but also as to the full scope of their intended application. Whereas some official statements in particular cases had been widely interpreted as insistence that only sale f.o.b. plant was lawful, a formal statement by the Commission during the controversy (one of several that expressed the same view) said, "The Commission does not advocate the imposition of a requirement that business enterprises price their goods f.o.b. mill or that they use any other form of geographic pricing practice. In the Commission's opinion, one of the principal virtues of the antitrust laws is the fact that they maintain freedom of choice and variety of behavior among businessmen, forbidding only the specific practices and conditions which have been condemned by law as destructive of competition."[22]

Most of the Commission's effort to redefine its position pertained to price discrimination, which it had previously considered, so far as territorial discriminations were concerned, almost wholly in setting of pricing formulas. However, it also gave further thought to its decision as to count two of the conduit case. Critics of the Commission had argued that in this case the decision as to count one had found that the producers conspired, while the

decision as to count two had condemned them for action that fell short of conspiracy, and that the two counts had been considered so different that two of the companies, though acquitted of violating count one, had been found to have violated count two. In a published notice to the staff early in the controversy, the Commission said:

"In the Rigid Steel Conduit case, the Commission found, and the circuit court agreed, that adherence to an industry-wide basing-point formula, with the knowledge that other concerns are adhering to it also, constitutes in itself a violation of the Federal Trade Commission Act by the individual adhering companies when price competition is thereby eliminated. It would have been possible to describe this state of facts as a price conspiracy on the principle that, when a number of enterprises follow a parallel course of action in the knowledge and contemplation of the fact that all are acting alike, they have, in effect, formed an agreement. Instead of phrasing its charge in this way, the Commission chose to rely on the obvious fact that the economic effect of identical prices achieved through conscious parallel action is the same as that of similar prices achieved through overt collusion, and, for this reason, the Commission treated the conscious parallelism of action as violation of the Federal Trade Commission Act. Should the Supreme Court sustain the Commission's view, the effect will be to simplify proof in basing-point cases, but to expose to proceedings under the Federal Trade Commission Act only courses of action which might be regarded as collusive or destructive of price competition."[23]

Later, in denying a motion to reopen the conduit case, the Commission said, "The Commission does not consider that the order in its present form prohibits the independent practice

of freight absorption or selling at delivered prices by individual sellers. What the questioned portion of the order does prohibit is continuance of the basing-point, delivered-price system, found to have been the subject of conspiracy, or any variation thereof which might be accomplished through the practices specified...when done, as stated in the order, 'for the purpose or with the effect of systematically matching delivered price quotations.'" [24]

The phrase "conscious parallel action," first used by the Commission in the interpretative statement quoted above, won subsequent wide use in discussions of existing and appropriate boundaries of the law. As will appear below, the Commission now proceeds against such parallel action without alleging that it is conspiracy.

As the political effort to amend the law subsided, it became clear that delivered pricing formulas were legally vulnerable under laws that would not be relaxed by amendment. Basing-point systems and zone pricing systems had been defined as two more of the various means of price fixing that from time to time appear and, when discovered, are struck down. Legal proceedings against them became part of the regular means of law enforcement. Such proceedings have been infrequent, perhaps in part because the established vulnerability of such systems made use of them less frequent. In 1964 the Sherman Act was successfully used against a group of producers of rock salt who had fixed delivered prices and artificially used rail freight in computing these prices though some of their shipments had been made by other means of transportation.[25] In 1967, in another basing-point case under the Sherman Act, a consent decree prohibited collusive use of any "freight-equalized multiple basing-point system" and also

prohibited each individual defendant from applying freight equalization to an f.o.b. factory price unless the buyer was given the option of buying at the factory at the factory price and arranging for his own transportation.[26]

In the early 1970's, delivered pricing formulas received renewed attention. The Commission investigated the basing point formula used by seven important producers of softwood plywood. In April 1974, it issued a complaint against five of them, which was awaiting trial when this memorandum was written.[27] In July, two more producers accepted consent orders against the same practice.

The pending complaint invokes a charge of conscious parallelism rather than conspiracy. It charges that the five producers are using a single basing point at Portland, Oregon, and applying all-rail freight from that point in selling plywood shipped from mills in various states, many of which are in the American south. The complaint alleges that rail rates are charged when shipments are made by cheaper modes of transportation; that buyers are denied the option of getting their purchases at the plants at f.o.b. plant prices; that identical and inaccurate weights are used as a basis for pricing, and that such practices result in receipt of substantial amounts of phantom freight. The substance of the complaint is that the practices of these mills are unfair and improper, not that they are instruments of price agreement. Though all five companies are respondents in the same complaint, the complaint does not charge that they have agreed to sell in this way. Instead, the charge is that "the respondents individually, and in combination with other companies, are now using and for a number of years have used and pursued parallel courses of business behavior constituting unfair

methods of competition and unfair and deceptive acts in commerce." The complaint comes no nearer a charge of price fixing than to say that the respondents have established "a system of delivered prices" and that one of the effects is "to stabilize prices and provide certainty in the pricing of softwood plywood among competitors."

The consent orders[28] (identical in content) are to become effective after orders against the five other companies have become final. They require that each company shall cease to use a basing point system; for 10 years shall give buyers the option of buying at the plant in quantities of at least a truck-load; shall state the amounts of actual freight cost on each invoice of plywood sold at delivered prices; shall stop using estimated weights unless these are based on prescribed types of experience, and shall stop reporting to other manufacturers its prices and terms of sale. A proviso explicitly authorizes freight absorption, allowances to meet lower prices of competitors, and uniform delivered prices within the normal zone of delivery by the seller's vehicle from a plant or distribution point.

Thus conscious parallelism has become, in the Commission, subject to decision not yet rendered in the courts, a fully established basis for corrective action, not only as a supplement to a charge of conspiracy or as a means to remove the momentum effect of a conspiracy, but in situations in which such considerations are not involved.

1V - SYSTEMATIC DELIVERED PRICING

Footnotes

1. Corwin D. Edwards, The Price Discrimination Law, Washington, D.C., The Brookings Institution, 1959, p. 364.

2. Ibid, Table 6, pp. 680-681. The table gives citations to the decisions. The decisions are to be found in 24 FTC 306, 27 FTC 225, 27 FTC 377, 31 FTC 706, 32 FTC 538, 35 FTC 201, 38 FTC 609, and 39 FTC 518. In one case the order was appealed; and in this it was modified and enforced. See Phelps Dodge Refining Corp. et al. v. FTC, 139 F 2d. 393 (2nd Circuit, 1943). Another of the orders resulted in a successful suit by the government for civil penalties; See 4 Statutes and Decisions FTC 822 (1947).

3. Ibid, Table 6.

4. For a summary of the case see ibid, pp. 370-371.

5. National Lead Co., 49 FTC 791 (1953) and 886.

6. National Lead Co. v. FTC, 227 F 2d. 825; (7th circuit, 1955) FTC v. National Lead Co., 352 U.S. 419 (1956).

7. I examined this file while I was a member of the Commission's staff and mentioned it publicly at that time, but without more detail than I have given here.

8. Cement Manufacturers Protective Association v. U.S. 268 U.S. 588 (1925) and Maple Flooring Manufacturers Association v. U.S. and 268 U.S. 563 (1925). In this early cement case the focus of attention was upon the industry's use of statistics. In the maple flooring case the focus was upon cost computation, and the industry's basing-point system was regarded by the court as so located relative to points of production that transportation costs from it approximated the actual costs incurred. See Edwards, op.cit., note 1, p. 355.

9. Zone pricing was condemned as part of a plan to stabilize prices in U.S. v. Linseed Oil Co., 262 U.S. 371 (1923); use of a basing-point system was part of the case in Sugar Institute v. U.S. 297 U.S. 553 (1936). See also U.S. v. Sugar Institute 15 F. Supp. 817 (S.D.N.Y. 1934).

10. 8 FTC 21 (1924). See also Edwards, op. cit., note 1, footnote on p. 353 which quotes testimony by a vice-president of United States Steel about the company's subsequent changes in its methods of pricing.

11. These developments are summarized, with appropriate citations, in Edwards op. cit., note 1, at pp. 356-363.

12. Corwin D. Edwards, "Doing Business Under the Present Law About Delivered Prices," Michigan Law Review, April 1945, pp. 743 ff.

13. Edwards, op. cit., note 1, Table 6, pp. 680-681.

14. For the Commission's decision see 37 FTC 87 (1943); for that by the circuit court, see Aetna Portland Cement Co. v. FTC, 157 F. 2d. 533; (7th circuit 1946); for that by the

Supreme Court, see FTC v. Cement Institute, 333 U.S. 683 (1948).

15. Regid Steel Conduit Association, 38 FTC 534 (1944).

16. Triangle Conduit and Cable v. FTC, 168 F. 2d. 175 (7th Circuit, 1948).

17. Clayton Mark & Co., et. al. v. FTC, 336 U.S. 956.

18. Ordinarily, in such a system a seller sets limits to the amount of freight that he will absorb by merely refraining from efforts to sell at the more distant destinations. Occasionally, however, such limits are stated as exact amounts. Occasionally, too, the method of pricing by which a similar result is sought is to quote buyers mill prices that include estimated maximum freight, but allow them deductions of the freight costs that they incur in shipping the goods to their destinations, up to a maximum specified amount. These variants are too infrequent, and their differences in result from the other ways of pricing are too small, to have given rise to well-defined legal concepts. Indeed, only one case involving a focus upon freight allowances resulted in an order during the years in which the Commission was most actively concerned about delivered pricing, and in this case several other price-fixing devices were also involved. See Sayles Finishing Plants, Special Fabrics, et. al., 49 FTC 427 (1953).

19. Edwards, op. cit., note 1, Table 6, pp. 680-681.

20. The controversy is summarized in ibid, pp. 400-438.

21. Quoted from a Congressional hearing in ibid, pp. 409, 412.

22. Quoted in ibid, p. 415, from a Senate committee document.

23. Quoted in ibid, p. 404, from the same document.

24. Docket 4452, Order Denying Motion to Reopen and Modify, July 7, 1949, quoted in Edwards, op. cit., note 1, p. 405.

25. U.S. v. Morton Salt Co., 1964 Trade Cases #71,198 (D. Minn. 1964), affirmed per curiam 382 U.S. 44 (1965). A parallel criminal indictment resulted, however, in acquittal.

26. U.S. v. Pennsalt Chemicals Corp., 1967 Trade Cases #71.982 (E.D.Penn., 1967).

27. Docket 8958. In the matter of Boise Cascade Corp., Champion International Corp., Georgia-Pacific Corp., Weyerhaeuser Company, and Willamette Industries, Inc., Complaint, April 18, 1974.

28. Dockets C-2518, International Paper Company, and C-2519, Vancouver Plywood Company.

V - PRICE DISCRIMINATION

The law against price discrimination originated from evidence in early cases about monopolization to the effect that large firms selling over wide areas sometimes reduced their prices locally against selected competitors, crippling the latter one by one without much injury to themselves. Section 2 of the Clayton Act, enacted in 1914, was intended to stop such practices.[1]

From its enactment until it was drastically amended in 1936, it was seldom used. The Department of Justice invoked it only as the basis for a supplementary charge in cases about violation of the Sherman Act, and in 22 years obtained judicial injunctions against only four violations.[2] During the same period the Federal Trade Commission invoked this law in 43 complaints, of which it dismissed 31; and of its 12 orders to cease and desist, four were reversed on appeal, seven were not appealed, and one was belatedly appealed after the law had been amended.[3]

The meagreness of the law's application was attributable largely to its limited scope. In 1923 the Commission lost the first of its cases that was appealed, when a circuit court held that Section 2 did not cover harm to competition in the buyer's market, and until the Supreme Court reversed this interpretation five years later in a private suit, this limitation reduced the field in which the law was applied.[4] Moreover, the law contained two explicit limitations. First, it did not apply to discrimination "on account of differences in the ...quantity of the commodity sold," and the courts interpreted this provision as a complete exemption of quantity discounts regardless of their amount. Secondly, the law exempted

"discrimination in price in the same or different communities made in good faith to meet competition." Though the required good faith was obviously absent where the seller's discrimination had a monopolistic purpose, it could be asserted in every case in which somebody other than the respondent, whether by discriminating or not, had initiated the low price and the seller had merely followed. If a discrimination was widespread, it could be attacked successfully only by a charge against its initiator, if the Government could identify him and prove that he acted first.

While this version of the law was in effect, the focus of concern about price discrimination changed substantially. In important parts of the economy, distribution of goods through traditional wholesale and retail channels was being rapidly replaced by use of other channels, among which corporate chains were the most prominent.[5] Organized small distributors tried to get state legislatures and the Federal Government to apply legal curbs to such developments.[6] In 1926 the Federal Trade Commission was directed by the Senate to make a comprehensive economic investigation of chain stores. The investigation resulted in 33 reports, culminating in a final one in 1934.[7] Though the Commission was impressed by various virtues of chain stores, it attributed to advantages that such stores had in buying, derived from price discrimination, "a most substantial part of the chains' ability to undersell independents." It recommended that the law be changed to facilitate corrective measures.

Ignoring substantive suggestions by the Commission about the content of such an amendment, the Congress drastically revised the law in 1936.

The new statute, the Robinson-Patman Act, had two substantive parts. One, in Section 3 of that Act, created criminal offenses, and was

ostensibly based upon the Canadian price discrimination law. The other amended Section 2 of the Clayton Act.

The Criminal Law

Three criminal offenses are created by Section 3. The second and third, which explicitly depend upon the discriminator's purpose, make it unlawful, for the purpose of destroying competition or eliminating a competitor, a) "to sell, or contract to sell, goods in any part of the United States at prices lower than those exacted by said person elsewhere in the United States" or b) "to sell, or contract to sell, goods at unreasonably low prices." The other, focussed upon the favoured buyer's advantage, makes it an offense knowingly "to be a party to, or assist in, any transaction of sale, or contract to sell, which discriminates ...against competitors of the purchaser, in that any discount, allowance, or advertising service charge is granted to the purchaser over and above any discount, rebate, allowance, or advertising service charge available at the time of such transaction to said competitors in respect of sale of goods of like grade, quality, and quantity."

The offenses that explicitly depend upon the seller's purpose are not defined with precision, but appear to include little, if anything, that is not already unlawful under the Sherman Act as an attempt to monopolize. (See Chapter V111 below.) The other offense is so defined that it covers only discrimination on like quantities at identical moments of time. As to these, it is applicable to any knowing participant, whether he is seller, buyer, or intermediary, and cannot be justified by difference in cost or by need to meet competitors' offers. What is a criminal offense thus seems to include much that remains lawful under the revised version of Section 2

of the Clayton Act, but to exclude some conduct which that Section makes unlawful.

In the 20 years after the Robinson-Patman Act, the Department of Justice instituted only five cases under Section 3, and in four of these the charge was supplementary to one under the Sherman Act. Nevertheless, the Department occasionally has invoked Section 3 against flagrant discrimination. In one such proceeding, a dairy company was found guilty of contracting with the country's largest food chain to pay the latter a secret rebate of $50,000 and thereafter to give that chain secret 11 per cent discounts on purchases.[8]

In another a national dairy firm was convicted for selling milk below cost in the Kansas City area with predatory intent.[9]

Efforts to use Section 3 in private suits have not been successful. In such a suit the Supreme Court held in 1958 that Section 3 is not part of the Clayton Act but a separate statute, and that private litigants cannot base upon violation of it claims for triple damages such as the Clayton Act makes available to persons injured by violation.[10] Subsequent to this decision, such private suits must be based upon violation of Section 2 of the Clayton Act, which has a different scope.

Section 2 of the Clayton Act, as Revised in 1936

Section 2 of the Clayton Act, as amended by the Robinson-Patman Act, is complex, both in purpose and in content. The amendment tried to blend two purposes: the traditional one of maintaining competition and a new one of making price relationships equitable for the persons involved. The committee report of the House of Representatives put first in its statement of

purposes "to restore, so far as possible, equality of opportunity in business," and the Senate committee's report used very similar language.[11] The House report elaborated the point as follows: "The existing law has in practice been too restrictive in requiring a showing of general injury to competitive conditions in the line of commerce concerned, whereas the more immediately important concern is injury to the competitor victimized by the discrimination. Only through such injury in fact can the larger, general injury result."

As amended, Section 2 contains anomalies that are difficult to understand. Some of them arise from effort to give equitable objectives the appearance of measures designed to preserve competition. Others are clearly attributable to haste in the legislative process. Various bills were exposed to nine days of hearings in the House, none in the Senate. At these hearings, the food industries were substantially represented, and so were a few other segments of the economy, but spokesmen did not appear for important parts of the economy that would be subject to the law. In each house of Congress, bills quite different in content were pieced together by compromise; in each house the result was passed before there was clear consensus by the majority about what was being done. Indeed, accepting a proposal that he had not had opportunity to appraise, one Senator said in debate: "I think it might be well, since it will probably be necessary to write the bill in conference, that all worth-while suggestions that may be offered should be incorporated in the bill so that the conferees may sit down and finally perfect the bill."[12] In fact, the conference committee of the two houses wrote the bill as enacted, performing hastily functions ordinarily performed slowly and carefully by working committees of each house.[13]

As finally enacted, Section 2 pertains to five separate types of violations, to which four different standards of illegality are applicable. Separate sub-sections cover i) price discrimination by sellers; ii) brokerage commissions; iii) payments for services accessory to sale; iv) provision of such services, and v) receipt of price discrimination.

Their nature expresses a major anomaly of the Act, inexplicable but pervasive: that, although the incentive for legislation was chiefly to curb use of bargaining power by powerful buyers, the chief means chosen was to curb discrimination by sellers, who were the targets and perhaps the victims of that power. Of the five subsections listed above, the first applies to sellers only; the second to sellers and buyers alike; the third and fourth to sellers only, and the fifth is so written that it is supplementary to the first and involves special difficulties in its application.

For convenience, these parts of Section 2 will be discussed here in a different sequence. The brokerage provisions, those related least closely to price discrimination, will come first. Then will come the sub-sections about payment for services and provision of services, which resemble each other. Then will come, successively, the more complex and more important provisions about price discrimination by sellers and receipt of discrimination by buyers.

Brokerage. In Section 2 (c) payments of brokerage fees or anything in lieu thereof are unlawful if made by a person on one side of the transaction of sale to a person on the other side.[14] The forbidden payment is unlawful *per se* unless it is made "for services rendered" in sale or purchase. If an unlawful purchase is made, the payer, the intermediate broker and the recipient violate the law.

This provision was aimed primarily at a practice in the food industries by which, in buying from suppliers who ordinarily distributed through brokers, chain stores and other buyers large enough to buy directly got price reductions equivalent to the brokerage payments that the direct purchases had made unnecessary. As enacted, however, the provision covered all similar transactions, large or small.

Early applications of this part of the law turned upon two key questions of interpretation. The first was whether the provision was a self-contained prohibition or, as part of a statute about price discrimination, should be construed in the light of the price-discrimination subsections. In the early cases the courts agreed that the provision was self-contained.[15] The other key question was what scope should be attributed to the phrase "except for services rendered." Respondents argued that they were exempt because they performed various kinds of services that justified the payments. With some initial hesitation, the courts uniformly disagreed, holding, in effect, that the law means that a buyer cannot serve a seller in the process of buying from him. As this view solidified, it became so strong that one court concluded that, though services were rendered and were useful to sellers, the exception did not make the payment for them lawful.[16] Thus, for practical purposes, the statutory phrase about services became meaningless.

A further question of interpretation, not so easily solved, is the nature of the "allowance or discount in lieu of brokerage" that

the statute forbids. A price concession to a buyer that is held to be a discount in lieu of brokerage is subject to tests of legality sharply different from those than applicable to it if it is merely a discrimination. If it is the latter, it is unlawful only if it is injurious to competition and is not justified either by difference in cost or as a way of meeting a competitor's price in good faith. If it is in lieu of brokerage, these considerations are irrelevant; it is unlawful if it passes from seller to buyer. Moreover, if it is a discrimination, the seller may have broken the law, but there is possibility that the buyer did not; whereas if it is in lieu of brokerage, both parties are violators.

Where a payment is identified by the parties as a substitute for brokerage, its nature is clear. Where the recipient receives the same percentage that is being currently received as brokerage by others, or that he formerly received as brokerage, this fact is convincing. The Commission and the courts have given weight to mathematical equivalence between the allowance and present brokerage to others or past brokerage to the recipient by a seller that has not wholly abandoned the use of brokerage. Illegality has been found where a seller's broker received a brokerage fee upon his own purchases and where a distributor's broker split the seller's fee with his principal for transactions in which the principal had bought from the seller without the broker's intermediation. Until recently, most cases in which the issues were raised were decided to be violations.[17] But where the computations are confusing, there is no clear rule. In 1956, a wholesaler of fish that sold to most customers through brokers who received a 5 per cent fee, sold directly to a few customers. In a third of the transactions with one such direct-buyer, price reductions were from 4 per cent to 6 per cent. Emphasizing that fish were perish-

able and subject to price fluctuations, the Commission dismissed the complaint.[18]

After the brokerage provision became law, it was promptly applied against Atlantic and Pacific Tea Company, the chain whose buying practices were typical of those at which it was aimed. Before the law was passed, A. & P. had regularly demanded brokerage fees because by purchasing through field buyers it made the use of brokers unnecessary by its suppliers in selling to it. After enactment of the law it had demanded net prices or quantity discounts equivalent to its former fees, or else payment of the fees into escrow accounts pending decision about their legality. In the proceeding, A. & P. argued that its brokerage was justified by the seller's saving of brokerage expense, and that its field buyers rendered numerous services to its suppliers. The Commission rejected both arguments. So did the Third Circuit, which held that the services were merely incidental and that, though the sellers' savings covered the brokerage, to accept the claim of cost justification would frustrate the purpose of the provision.[19]

After losing the case, A. & P. tried to retain its advantage by other means: a) buying a seller's entire output of a particular commodity; b) buying goods substantially different in quality from those the seller sold to others; c) buying for private branding at prices below those of the manufacturer's brand; d) buying from sellers who did not use brokers, and sometimes requesting that suppliers stop such use. In the 1950's, after the brokerage case had been followed by criminal and civil proceedings under the Sherman Act and by a consent decree in the civil proceeding, A. & P. had changed its buying practices. It had increased vertical integration and sale of private-label merchandise. Its purchases apparently were made with less effort to buy in bulk, with closer check upon quality,

and with frequent small purchases, more emphasis upon immediate delivery, and some purchases through brokers.[20]

Most of the brokerage cases, however, have not involved chain stores or advantages for similar powerful buyers. They have pertained to a) voluntary groups of independent firms (some of which were comparable to corporate chains in size) and cooperatives formed by such firms;[21] b) market information services that included performance of brokerage functions;[22] c) brokers affiliated with particular buyers;[23] d) firms that combined brokerage services with purchases for themselves,[24] and e) so-called resident buyers.[25] Many of these firms were small and lacked economic power. Some of them were engaged in activity that seemed unlikely to reduce competition and may have enhanced it.

The cases that involved voluntary groups and cooperatives forced substantial changes upon organizations that were widely regarded as effective ways in which small independent firms could become, by collaboration, effective competitors against corporate chains. These groups had financed their collective activities largely from brokerage fees. Effects of the cases upon the size and vigour of such groups were not uniform. One such group disintegrated; two were reduced substantially in membership, sales, and income; one changed methods without visible reduction in well-being; one, that had been losing strength during dissention about how to adjust to the law, grew in strength after the order against it. Private brands sold by such groups were promoted less vigorously and decreased in relative importance. The proportion of direct purchases by members of the groups usually increased.[26]

Few cases involved market information services. In these, a seller of market information

had been including in his service readiness to buy for his clients on request goods about which he had given them information; had collected on such purchase brokerage from the sellers; and had credited the brokerage to the clients as offsets to amounts they paid for the information. Stoppage of the collection of brokerage raised the cost of the information to the clients. The information services adjusted themselves to the stoppage, and continued to buy for their clients without collecting brokerage.[27]

Brokers affiliated with buyers were of several kinds. Some were brokers that did an ordinary brokerage business, but collected brokerage not only on transactions as to which they performed normal brokers' functions but also on transactions by the firm affiliated with them. Others were "dummy brokers," that is, they were used only or chiefly to obtain commissions on transactions by a particular buyer and had been established for that purpose. Of these, some were devices to divert funds from a business enterprise to individuals who constituted the brokerage firm; some were quasi-fraudulent in that they concealed their affiliation from the payers of the fees, and some received fees with the knowledge of the payer, who acquiesced in the buyer's use of this method to obtain a concealed discount. After such cases, brokerage payments to affiliated firms ceased. Sometimes firms that had been deceived stopped trading with the deceiver. Sometimes an ambiguous affiliation was terminated by sale of the brokerage firm to new owners.[28]

Buying brokers usually represented as brokers distant sellers that made many of their sales in lots smaller than carloads. Examples are some West Coast producers of fish products for Eastern markets. Such brokers found it advantageous to pool purchases so that shipments

could be made in carload lots. With early buyers reluctant to wait for later buyers to complete a pool car, the broker resorted to a simple expedient - purchase of the rest of the carload himself, to be sold while the goods were in transit. Sometimes there were additional advantages if the broker was officially the buyer of the whole carload, for if so, the shipper could rely upon the broker's credit, which he knew, without trying to keep track of the credit of changing groups of small buyers. Moreover, both shipper and broker could thus avoid problems that might arise if a buyer who had bought part of a pool car were to die, go bankrupt, or refuse to take delivery during an argument with the seller. Such incentives resulted in development of buying brokers, firms that still regarded themselves as brokers but took title to substantial parts of the goods they sold. Some of them increased their wholesaling functions and reduced their activity as brokers as they acquired clientele and capacity to cope with the risks and costs of marketing. Though this fluid relationship of intermediary, seller and buyer was not inherently either discriminatory or anticompetitive, it was not permissible under Section 2 (c). Termination of it by order appears to have had two consequences: first, more frequently than before, distant producers, no longer able to rely on buying brokers as keepers of stocks of goods, established their own consigned stocks near their distant markets. Secondly, in some parts of the country, particularly the southeast, intermediaries who had been buying brokers experienced increased difficulty in serving their small customers, and suppliers found that corporate and voluntary chains were more attractive than before, relative to small retailers, as means of reaching markets.[29]

Resident buyers were chiefly buyers of garments. The provision about brokerage, though

written in ways relevant to the structure of food distribution, is applicable to all industries. It fits the garment industries badly. These industries have been long concentrated in a few metropolitan centres, where much of their production is done by small firms. Distributors elsewhere have kept in touch with these centres through resident buyers - agents of the buyer who watch styles and buy for him. Though such buyers sometimes have been paid by the distributors, more often they have received their pay from producers of garments as percentages of their purchases. When they do so, they and the producer clearly violate the brokerage provision. By the close of the 1950's, the Commission had issued 13 orders against unlawful brokerage in these industries, and two of the orders had reached the courts and been sustained. Since the industries have been highly competitive, it is probable that the source of the resident buyer's fee is taken into account in the bargaining of these industries, so that no reliable advantage is obtained by buyer or seller from the fact that the other pays the broker's fee. Certainly the Commission has received no substantial number of complaints from the industry about brokerage.[30] The impact of the brokerage provision upon the industry was that of an attempt to change a well-established trade practice with no evident public purpose. The cases appear to have reduced somewhat the frequency of payment of fees by sellers, and to have evoked efforts to conceal such payments. Nevertheless, if the Commission were to enforce the provision systematically, it probably could develop enough cases to occupy the full time of its staff.

During the last 15 years, several cases have been decided in ways that do not fit the rigid interpretation of the brokerage provision that had developed during the previous quarter

of a century. They seem to point toward a closer relationship between that Section and the standards of other parts of Section 2. However, these cases have not yet formed an intelligible pattern and do not provide reliable precedents.

The stimulus for the change appears to have been the Supreme Court's decision in 1960 in the Broch case, the first brokerage case to reach that Court. The substance of the decision was orthodox - condemnation of reduction in the brokerage fee as a vehicle by which pressure by a large buyer had obtained a discriminatory price reduction. But the decision was five to four, and the language of the majority put life into issues that had been dead or quiescent. It emphasized the point that the fee had been reduced to get a particular order, and distinguished this discriminatory deviation in the fee from non-discriminatory reduction of such a fee. It treated the relationship between the low price and the brokerage fee as one that needed proof and did not "automatically" compel the conclusion that brokerage had been passed to the buyer. Moreover, it said that if the buyer had rendered service to the seller, which had not happened, this would have been "quite a different case."[31]

The unsettling effect of the Broch decision has become evident as to cost justification. The problem arose in a case in which a complaint by the Federal Trade Commission alleged violation in that discounts systematically given to large customers were derived partly from systematic reduction of fees to brokers in sales to such customers. After considering cost information offered in defense, the Commission condemned the discounts because these were not completely covered by savings other than those from reduced brokerage fees. The Fifth Circuit set the order aside in a decision that reached beyond the Broch case

precedent. It held that the Commission must consider all cost reductions and that if these justified the discounts there was no violation of the brokerage provision. Thus it appeared to make cost defenses fully relevant to brokerage cases. The Commission then dismissed the case and published a memorandum interpreting the court's decision as meaning that the Commission "must not rely solely on the fact that the seller paid less brokerage on the sales at the lower price, but must establish a casual relationship between the reduced brokerage and the reduced sale price." The memorandum interpreted the rest of the appellate decision as dicta with which it did not necessarily agree.[32]

In another recent case, such a controversy about costs has affected application of the brokerage provision to cooperatives. In the orthodox way the Commission condemned as discounts in lieu of brokerage price reductions received by a cooperative that bought at reduced prices, charged its members more, and subsequently refunded to them as patronage dividends whatever excess receipts remained in its possession. The decision held that the discounts were clearly allowances to the buyers and that there was no point in segregating savings to rebut the implication that these allowances constituted transmission of brokerage fees. One Commissioner dissented, arguing that under the Broch decision discounts were lawful if they were based upon savings other than brokerage. The Seventh Circuit reversed on the same ground, holding that the cost data of the case showed that the discounts were not in lieu of brokerage.[33] This decision is consistent with the Commission's memorandum, quoted above, interpreting the Fifth Circuit's decision, but not with what the Commission called the dicta of that decision.

The Broch case has also had an unsettling effect upon decisions about the performance of

services by intermediaries. This effect has come, not from decisions reconsidering Section 2(c)'s exception as to services rendered, but from decisions as to whether services were broker's services subject to that section or functional services subject to Section 2 (a). The problem developed in two settings, a private suit decided in the courts and a public case decided by the Commission.

In the private suit, a rayon firm, having been denied by a manufacturer of yarn, a place as one of that manufacturer's jobbers, challenged the discounts to jobbers as allowances in lieu of brokerage. The district court granted a motion for summary judgment for the defendants. The Second Circuit first reversed the decision; then, after rehearing, decided that the discounts should be appraised under Section 2 (a). Having invited the Commission to submit its views, it approved the Commission's view that the intermediaries were independent firms that facilitated acquisition of yarn by small buyers and that reliance upon Section 2 (c) might well "render all functional discounts illegal per se."[34]

Similarly, but more cautiously, the Commission has decided a charge under Section 2 (c) by considering whether or not there was damage to competition. An intermediary for food products, that sold to wholesalers only and thus competed with brokers, took title to the goods it bought, and obtained from its suppliers discounts that were equal to the fees paid to brokers by these suppliers and that sometimes were so described in the business documents. A majority of the Commission decided against the complaint in a decision of which the first version (afterward modified) rested squarely on a finding that the challenged activity was not anticompetitive.[35]

Subsequently, however, the Commission reverted toward its previous types of analysis.[36]

<u>Allowances and Services in Distribution.</u> Section 2 (d) forbids payment of anything of value to customers for services rendered by them in distribution unless the payment is available on proportionally equal terms to all who compete with them in distribution. Section 2 (e) applies a similar requirement of proportionality to provision of services or facilities to distributors. Though these provisions obviously were intended to be parallel, as enacted they had differences in wording that appeared to be important, but that the courts have deprived of significance by interpretation.[37]

The concept of distributive relationships that underlies these sub-sections differs fundamentally from that which underlies the brokerage sub-section. Whereas Section 2 (c), as interpreted, means that a seller or his agent cannot provide significant service to buyers in connection with purchases, and neither can a buyer or his agent do so for sellers, Section 2 (d) and 2 (e) presume that seller and buyer have joint interests in distributing goods and can aid one another in this work in various ways. (A third somewhat different concept, which will be discussed below, appears in application of Section 2 (a) to functional discounts to distributors.) Hence Sections 2 (d) and 2 (e) seek, not to forbid aid or payments for aid in distribution by parties on opposite sides of distributive transactions, but to require fairness in apportionment of that aid or those payments.

Like the brokerage sub-section, Sections 2 (d) and 2 (e) are applicable without need to show any anticompetitive effects; and they provide no right for violators to offer a defense that their action was justified by cost differences. Unlike the brokerage sub-section,

however, the activities that are subject to challenge are only those of the firm that provides the allowances or services, with no mention of equivalent liability for the recipient thereof. At one time, powerful buyers took advantage of this apparent loophole in the law by seeking discriminations in the form of allowances and services instead of in other forms,[38] but beginning in the 1950's the Commission proceeded against recipients of allowances and services as violators of Section 5 of the Federal Trade Commission Act.[39] Thus, by supplementary use of another statute, policy as to allowances and services has been made applicable to both producers and distributors with substantial symmetry.

The purpose of this part of the law is to prevent three types of discrimination: a) payment to distributors for services that have not been performed; b) payments that greatly exceed the value of services performed, and c) denial to distributors of payments or services that are provided for their competitors.

"Proportionally equal terms," the relationship that makes allowances and services lawful, is not defined in the statute. Rejecting other plausible meanings for the phrase,[40] the Commission and the courts have applied the law as though the provision requires that the services, facilities, or allowances that the supplier provides to distributors that compete with one another must be proportional either to the relative value of purchases by these distributors or to the relative number of units that they buy.

To conform to the law, a supplier that wishes to provide an allowance, service, or facility to any individual distributor must ascertain if any of his other distributors

compete with that one. There may be difficulties in deciding whether or not peripheral firms are part of the competing group. Such difficulties have grown, for in 1968 the Supreme Court decided that if a supplier sells directly to retailers as well as to wholesalers, his obligation to give proportional treatment exists not only to retail customers who buy from him directly but also to customers of his wholesale customers that compete with the direct-buying customers.[41] Identification of such indirect customers and determination of the scope of their competition is obviously no easy task.

Having identified the group of distributors that must be proportionally treated, the supplier must develop allowances and/or services that can be proportionally provided. Proportionality is not required for each kind of service considered separately, but for the entire combination of services and facilities as a group.[42] A supplier who gives an allowance to a large distributor for the distributor's television advertising or newspaper advertising must make a proportional allowance available to competitors of that distributor who are too small to advertise in such ways. He may do this by appropriate offers for window displays, handbills, or other types of advertising that are within the small firm's reach. Similarly, if the supplier sends a demonstrator to sell his product for a department store, he must offer a proportional equivalent to stores too small to use demonstrator service - perhaps in the form of a display cabinet.

The services and facilities that may be thus combined in an offer to distributors can be various, and the combinations of them can be complex. The task of determining whether or not the requirement of proportionality is met by a particular combination of offers becomes

one of estimating whether or not what is offered to different recipients includes something that each can use to a comparable degree and that costs the offerer an approximately proportional expense to supply. No precision is possible in such appraisals. However, gaps that contain nothing and offers that are grossly disproportionate can be identified.

To promote conformity to the law, the Commission issues, and from time to time revises, a pamphlet guide.[43] This states simply and in detail each element of the law's requirement, and illustrates each by brief hypothetical examples. This general guide is supplemented in two ways: first, in industries such as that for cosmetics, in which relevant distributive relationships are numerous, the Commission, after consulting the industry, formulates trade practice rules that, though without formal legal effect, set forth interpretative applications of the law to conditions of that industry. Secondly, the Commission makes available an advisory service that, upon request, examines a supplier's contemplated program as to allowances and services, and says whether or not anything in it appears to be legally subject to question, and if so, in what respects. The impact of this part of the law consists, in practice, largely of influence upon business practices exercised by such informal means. Formal legal proceedings appear, however, in two ways: the Commission uses such proceedings where it thinks that a supplier is flouting the law or seriously misinterpreting it. Private firms sue other firms for injunctions or for triple damages.

A seller's obligation under the law reaches further than selection of appropriate allowances and/or services. He must give adequate notice to each distributor that these aids are available, and he would be wise to

have evidence of the notice in writing.[44] He must find ways of assuring that distributors newly acquired are aware of the aids available to their competitors, and that all competing distributors are informed of each change in the terms on which aid is offered. If any part of the aid is conditioned upon performance by the distributor - e.g., upon advertising by him that mentions the supplier's product - the supplier is required to take reasonable care to be sure that the condition is actually fulfilled.[45] Thus a well-considered plan and considerable effort are necessary to a seller who tries to comply with the law, and the Commission's task of assuring compliance involves substantial amounts of surveillance.

This part of the law appears to have reduced intentional discriminations that once arose from pressure by powerful buyers to get indirect advantages. One part of the problem created by such discriminations appears, however, to escape the law's impact. It arises from the fact that the total volume of business done in a single type of product by large distributors sometimes exceeds that done by some of their smaller competitors by considerably more than is necessary to obtain the maximum allowances and services available from the individual suppliers. Where this is so, a large distributor may get maximum available allowances and services from several suppliers, and thus, without advertising and selling in a way that differs substantially from the way that he would otherwise choose to do business, may obtain from his suppliers a substantial portion of his advertising budget or his sales expense, while to get the proportional equivalent each of his small competitors may have to choose which supplier will receive his cooperation, and thus may have to modify his selling practices appreciably.[46]

In one respect, too, Section 2 (d) and 2 (e) appear to distort sales effort wastefully. Some advertising and selling consisted, when these provisions were applied to them, in buying or providing services that were selectively useful to the supplier without spending proportional funds upon less useful effort. In such instances, the law's requirement of proportional equality imposed upon the spender an unwelcome choice between ceasing to spend for what he needed and continuing to do so by adding to his expenditures funds for additional activities that were not worth their cost.

Two instances illustrate such situations. The first is the case of Kay Windsor, a dress manufacturer. Producing dresses that depended for their appeal upon style, which changed seasonally, Windsor could induce many dress shops to buy Windsor dresses if large department stores and certain shops with prestige bought and advertised them early in each dress season. Therefore, Windsor offered advertising allowances selectively to particular distributions. Thus it violated Section 2 (d). After the order against it, it converted its selective allowances into proportional allowances, apparently with adverse effects upon the willingness of small buyers to buy the Windsor dresses.[47]

The other case is that of Holzbeierlein, a small baker in the District of Columbia who tried to advertise there economically in competition with larger bakers. His method was to pay allowances for preferential sales effort by a large local food chain. An order by the Commission terminated the arrangement. Nine years later Holzbeierlein's business was liquidated.[48]

Price Discrimination by Sellers. The conception of discrimination by sellers set forth in Section 2 (a) is explicit but limited. It covers discrimination in price in sale of commodities by a single seller to more than one buyer for use or resale in the United States. It does not cover discrimination in the price of services, in leases or consignment transactions, or in export trade. It explicitly allows sellers to choose their customers, though by refusals to deal such choices can be important means of discrimination.[49]

The core of its prohibition is that sellers are forbidden "to discriminate in price between different purchasers of commodities of like grade and quality ... where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent[50] competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them." Other parts of the Section contain an exemption for cost-justified price differences (which will be discussed below), an authorization for selection of one's own customers, and an exemption for price changes through time in response to changing conditions.[51] A procedural sub-section that follows - Section 2 (b) - authorizes the seller to rebut a case by showing that a price reduction was made in good faith to meet a competitor's equally low price. (This authorization also will be discussed below).

Since discrimination is forbidden only as to commodities of like grade and quality, application of the law involves initial problems about the treatment of non-standard goods. The extent of physical differences in commodities

and the evaluation of these differences by users are relevant to decision whether or not differences in the prices charged by the seller should be deemed discriminatory. Where there are minor differences in product, apparently not considered important by consumers, they are likely to be considered an insufficient basis for exemption.[52] The Commission has consistently held that difference in brand names, without significant difference in characteristics, is not a difference in grade and quality.[53] In the Borden case a price difference was challenged where, without difference in the physical characteristics of the product, consumers treated the brand as important. Reversing the circuit court, the Supreme Court held that branded evaporated milk identical with private label milk that the producer sold at lower prices did not attain difference of grade and quality by bearing a widely desired label. It considered that consumer preferences were relevant to the law's provisions about injury to competition rather than to the existence of discrimination.[54]

Discriminatory prices by a seller are potentially unlawful if they probably are injurious to competition in ways specified in the law. Two kinds of injury are distinguished. The first, substantial lessening of competition or tendency toward monopoly, pertains to effects that are likely to reduce competition in the market as a whole - for example, discrimination that cripples important competitors. The second pertains to injury in a different sense - injury to the competitive opportunities of firms that incur disadvantage from the discrimination. This type of injury incorporates the equitable purpose that the amendment brought into the Act. Impairment of the competition of a disadvantaged class of buyers can be unlawful regardless of its effect upon market competition. If, for example, buyers

favoured by a discriminatory price replace buyers that pay the higher price, competition by the victims of the discrimination has been destroyed, but competition in the market may be as vigorous as before. Hereafter the first type of injury will be called injury in the broad, or market, sense; the second type, injury in the narrow, or equitable, sense.

If a discrimination probably would create either type of injury, it is unlawful unless one of the statutory grounds for exemption is applicable to it. Neither type of injury makes the discriminator more vulnerable than the other, nor gives the Commission power to apply a remedy that is not available for the other. Thus, in applying the law the Commission has no incentive to distinguish the types of injury precisely. Its complaints usually have alleged the narrow type of injury, sometimes both types, and seldom the broad type only. Since the narrow type is usually easier to prove, proceedings have tended to focus upon it whether or not the broad type has been alleged also. Findings in cases concerned with both types often have lacked careful distinction between the two types, and sometimes have found the broad type as well as the narrow without a clear basis for the broader finding.[55] Where the Commission's analyses have had such characteristics, respondents have had nothing to gain by insisting upon the distinction.

If the Commission proves that injury of either kind is probable, violation has been proved unless the respondent can show justification. Two types of justification are available: a showing that the price difference made only due allowance for difference in cost, and a showing that the low price was made in good faith to meet the equally low price of a competitor.

Section 2 (a) provides a cost defense in the following passage: "Nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered."[56]

These words were carefully chosen. Those who wrote the bill believed that sellers, with their overhead costs already covered by their existing business, were vulnerable to demands for price concessions that would get them additional business, and that large buyers exploited this vulnerability to buy at discriminatory prices. The report by the judiciary committee of the House of Representatives said that the language "precludes differentials based on the imputation of overhead to particular customers, or the exemption of others from it, where such overhead represents facilities or activities inseparable from the seller's business as a whole and not attributable to the business of particular customers or of the particular customers concerned in the discrimination."

The other type of defense - meeting competition in good faith - is less explicit in the statute. The two houses of Congress had disagreed about authorizing it, and the law included their compromise. This provided that "nothing herein contained shall prevent a seller rebutting the prima facie case thus made by showing that his lower price .... was made in good faith to meet an equally low price of a competitor." Though this provision made clear that respondents could introduce relevant evidence, it did not state the effect of such a showing. As will appear below, disputes arose about that effect; but the courts decided that when the showing is made in a case under Section 2 (a) it acquits

the respondent.[57]

Section 2 (a) is applicable to all kinds of price discrimination. Different kinds of discrimination - e.g., discrimination by quantity discounts, by volume discounts, by functional discounts, and by territorial price differences - have sometimes involved special types of injury to competition or special problems as to cost justification or as to meeting competition. What follows will discuss first the concept of injury to competition; then meeting competition as a defense; then due allowance for differences in cost. Where special problems arise from the peculiar character of the discrimination, these will be included in the discussion.

Injury to Competition: Discrimination may injure competition either at the level of the discriminating seller and his competitors (the primary line), or at the level of the buyer who pays the low price and his competitors (the secondary line). Where discrimination takes the form of functional discounts, the injury may also appear at the level of the disadvantaged buyers' customers (the tertiary line), and even at a fourth level, that of the customers of those customers.[58] At any of these levels, damage to competition may exist in any of the statutory degrees: tendency to create a monopoly, substantial lessening of competition, or impairment of the competitive opportunities of the buyers that do not benefit from the discrimination. Any of these kinds of damage at any level makes the discrimination prima facie unlawful. To identify clearly the considerations that have supported the decisions about injury is possible, however, in only a few of the cases, partly because many cases have been settled by consent orders or admission answers and therefore are based upon formal findings that are unrevealing, and partly because where the Commission has found more than one type of injury it often

has not distinguished them clearly nor related each to the part of the record of the case that supports it, and many of the decisions that are thus defective have not been appealed. What follows will be based, necessarily, upon the remaining cases.

Injury in the secondary line has been at issue in most of the price discrimination cases. The leading decision has been one by the Supreme Court in the Morton case.[59] Morton's salt was sold at volume discounts that enabled five large grocery chains to buy for $1.35 per case while customers who bought less paid from $1.40 to $1.60 according to the volume of their purchases. The Court found "obvious" that the substantial differences in purchase prices injured competitive opportunities. It said, "That respondents' quantity discounts did result in price differentials between competing purchasers sufficient to influence their resale price of salt was shown by evidence. This showing in itself is adequate to support the Commission's appropriate findings." To the objection that salt was too small a fraction of grocery sales to create injury, the Court replied that, "Since a grocery store consists of many comparatively small articles, there is no possible way effectually to protect a grocer from discriminatory prices except by applying the prohibition of the act to each individual article in the store." It held that a showing of a practice of selling substantially cheaper to some customers than to their competitors is "in itself sufficient to justify our conclusion that the Commission's findings of injury to competition were adequately supported by evidence."

With this authority, enforcement of the law of price discrimination has stopped barely short of the view that a seller's price difference between competing customers is prima facie illegal. Any substantial and sustained difference in

buying prices has been regarded as injurious. If the beneficiary of the discrimination reduces his prices in reselling, his competitors face the necessity of either losing sales or losing profits by reducing their own prices. If the beneficiary does not reduce his selling prices, he obtains larger profits that give him substantially larger resources capable of use for greater sales effort or some other means of attaining competitive advantage. Since prevention of competition is enough to constitute the forbidden injury, proof that competitors of the beneficiary are numerous and strong is likely to be held insufficient to overcome such an analysis, for without the discrimination they might be more numerous and stronger. Similarly, proof that the beneficiary's competitors are making profits and growing larger is likely to be held insufficient, since but for the discrimination they might be making more profits and growing faster. In the Moog case, in which the beneficiaries of the discrimination did not reduce their own sale prices, customers of the discriminating seller that paid higher prices testified that they had not been injured by the discrimination. The Commission dismissed the testimony by finding that the discrimination was larger than Moog's discounts for cash, which the same customers thought important. In confirming the Commission's decision, the Eighth Circuit said that the fact that some buyers paid more than their competitors "constitutes an adequate evidentiary basis to support the Commission's finding that the price discriminations may substantially injure competition." As to the contradictory testimony, the court said, "their answers were conclusions contrary to simple mathematics .... A witness cannot be allowed by conclusions to deny a mathematical fact, and all the testimony of these jobbers, on this score, amounts to - if they understood the facts - is that they are not objecting."[60]

Where the price difference is territorial, the Commission qualifies its view of injurious discrimination. Early cases that involved discrimination of this kind developed in a setting of price fixing, in which the Commission appropriately held that the pricing formulas that it attacked were being used to injure buyers by denying them advantages from location near the plants of their suppliers; and in these cases the Commission defined prices as the net realizations by the seller at the point of origin of the goods. Later, in considering cases untainted by conspiracy, the Commission modified its view. It recognized that when purchasers are differently located, competition between those that pay different prices may exist only in limited areas or only on the fringes of sales territories, and that therefore the concept of injury developed in the Morton salt case was not necessarily appropriate to territorial discrimination. It redefined price to mean the price at whatever point (whether at the buyer's location or at the seller's plant) was appropriate to the transaction, and it came to recognize that where there were advantages of location neither buyer nor seller had a clear right to these advantages.[61] In 1957, a senior member of its staff expressed thus its policy toward territorial price differences: "...the law hits at the practice of throttling local competition by lowering prices in one geographic area while maintaining prices in other areas. It seeks to prevent a large seller, with an interstate treasury, from subsidizing a diminution or complete elimination of profits occasioned by discriminatory price cutting in one area, by maintaining - or perhaps raising - its normal profitable pricing structure in other areas .... The area of the price discrimination must represent .... a substantial portion of the over-all sales of the injured competitors."[62]

Where the price difference arises from functional discounts, peculiar difficulties have arisen in formulating the concept of injury. A firm may differentiate its prices to wholesalers from its prices to retailers; for because retailers do not compete with wholesalers, different prices at different functional levels are not considered injurious. There are, however, distributors that operate at more than one level. Chain stores, like wholesalers, buy directly from producers, but compete at retail with retailers who buy from wholesalers. In these and other relationships, competing firms may receive different functional discounts, and the differences may raise problems of injury.

When direct and indirect buyers compete, the concept of injury is difficult to apply. The law holds discriminators responsible for injury not only to the buyers discriminated against, but also to the customers of those buyers. Thus a producer becomes liable for the effects upon competition among retailers that may arise from the size of the difference between his prices to wholesalers and his prices to direct-buying retailers. In the Curtiss case low price to certain firms that bought directly from Curtiss gave these firms advantage over others that bought through intermediaries, and the Commission found the advantage injurious to competition.[63] In the Standard Oil case, an important part of the Commission's complaint was that price reduction to a jobber had been so large that part of the reduction had been passed on to retail customers of that jobber, who then had a buying advantage over retailers who bought directly from Standard.[64] The Commission attacked this as discriminatory. In such relationships, unlawful discrimination lies on either side of a knife-edge of appropriate relationships between prices to buyers at differ-

ent distributive levels. Unless the supplier controls the prices at which intermediaries resell to firms that compete with his direct buyers, he cannot assure that there will not be discrimination in favour of one of these two kinds of competitors. Yet for him to undertake such control is to engage in resale price maintenance, a practice contrary to the general policy of the antitrust laws.

The difficulty was evident in the Commission's order in the Standard Oil case, which required that Standard not discriminate "by selling such gasoline to any jobber or wholesaler at a price lower than the price which respondent charges its retailer-customers who in fact compete in the sale and distribution of such gasoline with the retailer-customers of such jobbers or wholesalers, where such jobber or wholesaler resells such gasoline to any of its said retailer-customers at less than respondent's posted tank-wagon price or directly or indirectly grants to any such retailer-customer any discounts, rebates, allowances, services, or facilities having the net effect of a reduction in price to the retailer." Commenting on this part of the order, the Seventh Circuit pointed out that Standard could not control jobber resale prices, and that the order gave Standard the choice of eliminating its wholesale discounts or using its right to choose its customers to refuse to sell to wholesalers whose resale prices were below its own price to direct-buying retailers.[65]

Where injury has consisted of damage to competitors in the primary line, the cases may be divided into two groups. In one group, there was evidence of predatory intent by the seller, or the seller so dominated the market that damage done by the discrimination clearly tended to consolidate that dominance.[66] In

the other group, the damage done by the discrimination consisted merely of diversion of business to the seller from the seller's competitors, so that its impact was scarcely distinguishable from that of price competition itself. In such cases, decisions have not been consistent, and have involved recurrent differences between the Commission and some of the appellate courts. The Commission has used the controversial view of injury with considerable consistency. In one case, it explicitly rejected an analysis by one of its hearing examiners that limited primary-line injury to injury of the broad type.[67] In 1951, it said that, "The very nature of quantity price differentials is to divert business to the seller granting such differentials, and, insofar as they cannot be justified by cost differences or otherwise defended, any substantial injury to competition due to them falls within the ban of the Act."[68]

In 1965, after the decision that included the foregoing quotation had been overruled on appeal, the Commission qualified only slightly its view of the scope of such injury: "A finding of substantial competitive injury on the seller level is warranted ... where the evidence shows significant diversion of business from the discriminator's competitors to the discriminator or diminishing profits to competitors resulting either from the diversion of business or from the necessity of meeting the discriminator's lower prices, provided that these immediate actual effects portend either a financial crippling of those competitors, a possibility of an anticompetitive concentration of business in larger sellers, or a significant reduction in the number of sellers in the market. In such a situation, the finding of possible competitive injury is not bottomed solely upon the fact that there has been or may continue to be diversion of business or loss of profits. Instead, the emphasis is

placed upon the reasonably foreseeable results of the diversion or loss of profits."[69]

The courts have not accepted such a view without various qualifications and some rejections. In the case that contained the Commission's statement just quoted, the Seventh Circuit rejected the Commission's decision about injury in the primary line, criticized it as based upon "questionable analysis and insubstantial evidence," and concluded that as to the primary line there was neither proof of discrimination nor proof of injury to competition or competitors.[70] In the Anheuser-Busch case the same court held that Section 2 is "not concerned with mere shifts of business between competitors," but required that the Commission prove "substantial impairment of the vigor or health of the contest for business."[71] In a private suit the Ninth Circuit saw no injury in territorial discrimination in the price of ice cream to recover a market share that had decreased from 25 per cent to 17 per cent in four years. It thought the discriminating firm's action a "realistic response to previous changes by others in the field, either in the locality or elsewhere."[72]

The law about injury is so written that if a discrimination results in probability of either the broad or the narrow kind of injury at any level - primary line, secondary line, or tertiary line - the price difference is <u>prima facie</u> illegal. Critics often allege that what creates narrow injury in the secondary or tertiary line may be pro-competitive in the primary line in that an oligopoly is weakened and its prices made more flexible by discriminatory price reductions and retaliation against them. So far as this may be true, its truth has no apparent relevance in administering the Act, for there is no statutory provision for evaluating against each other effects that may differ

in their impact on competition.

Meeting Competition: At first the Commission interpreted the part of the statute that gave discriminators the right to show that they had met a competitor's low price in good faith as merely a way of making available certain evidence relevant to the probability of injury. The legal effect of such a showing was first explored intensively in the Detroit gasoline case. Standard Oil Co. of Indiana had cut the price of gasoline to four firms by classifying them as jobbers, though one sold wholly at retail and the others sold partly so. One of them reduced its retail prices; another gave some of its retailer-customers part of the reduction in lower prices and in various other forms. The Commission found injury in the secondary line, and ruled that since injury had already appeared there was no need to consider Standard's defense that competition had been met in good faith. Reversing the circuit's affirmation of this decision, the Supreme Court held five to three that good faith in meeting competition is a complete defense, and remanded the case for appraisal of that defense as offered by Standard. With two dissents, the Commission rejected the defense on the grounds that Standard, knowing that the discriminatory prices were potentially injurious, had not tried to change its price policy after the Robinson-Patman Act became law; that the low prices expressed Standard's pricing policy, not a departure from it to meet a particular situation, and that, since all of Standard's major competitors used similar prices, recognition that any of them was in good faith would make the same defense available to the others and eliminate the need for any of them to establish non-discriminatory prices. The Seventh Circuit rejected the Commission's analysis. It saw in the record proof that the lower prices were departures from a non-discriminatory scale; saw

no reason why one firm should be denied a defense because others might also use it; thought that Standard's knowledge of the probability of injury was irrelevant, and thought that if the lower prices were originally made in good faith there had been no duty to revise them when the law was enacted. The Supreme Court affirmed the circuit court's decision on narrow grounds: that where the assessment of facts by a lower court is not arbitrary and unreasonable it will not be overturned on appeal.[73]

Though this case established the legal sufficiency of the defense, it also illustrates the narrowness of the exemption that is thus provided. Good faith is obviously absent if the purpose of the discriminator is to eliminate or reduce competition, or is similarly aggresive rather than defensive,[74] or if the price reduction precedes rather than follows the low price by others or continues after lower prices by competitors are known to have lapsed. The defense has also been found inadequate where the discriminator had sufficient knowledge that lower prices were actually available from competitors.[75] A firm may not meet competition if it has reason to know that the price being met is itself unlawful.[76] Moreover, the right to meet a lower price does not include a right to charge a price still lower, or to make the reduced price available for types of transactions more extensive than those for which the competitor's price is available.[77] This limitation has been interpreted to forbid reduction of the price of a premium brand to a level that eliminates or significantly reduces the customary price difference between that brand and competitors' products.[78] It is clear that the defense is available only for retaliatory departures from a non-discriminatory pricing policy, but how much breadth and persistence through time this requirement permits is far from clear.[79]

Due Allowance for Difference in Cost: The purpose of the cost provision in the law was stated explicitly in the conference report by the Congress: "The bill assures to the mass distributor, as to everyone else, full protection in the use and reward of efficient methods in production and distribution."[80] As formulated, the provision was not wholly appropriate to this stated purpose. In making price structures unlawful when price differences hurt particular classes of buyers and cannot be cost-justified, but leaving them lawful when prices do not vary with differences in cost, the provision encourages establishment of price structures that, if measured by relative costs, would be biased toward undue uniformity. This encouragement is enhanced by the fact that computation of cost differences is a task so expensive and complex as to discourage attempts to undertake it and to make success in it very difficult.

The cost provision is defective as means to efficiency in additional ways. In explicitly forbidding cost justifications that depend upon re-allocations of overhead costs, it creates a legal obstacle to efforts to use adjustment of the relative prices of similar goods to different kinds of buyers as a means of diminishing the amount of idle capacity and making fuller use of equipment. It discourages experiment with differential pricing as a means of improving proportions in the amounts of goods produced or distributed jointly and thus reducing their total cost; for it deprives of legal protection any such experiment that fails to achieve the intended result or that, though the total costs are reduced, does not also achieve differences in costs at least equal to the price differences that are used as incentives to competing buyers to purchase in different proportions.

These limitations are aspects of the deliberate preference of antitrust legislation for

competition over efficiency so far as the two are not compatible. The only additional feature here is that the law of price discrimination has not only competitive but also equitable purposes.

The lawmakers probably assumed that relevant cost information was available or could be readily obtained, and underestimated the difficulty of comparing price differences with cost differences. Cost information segregated by products is seldom available to American business.[81] Where such information exists, the task of allocating it properly is difficult. Moreover, since price differentiations usually arise because of differences in buying strength and in degree of competition rather than because of differences in cost, the task of cost justification typically consists in _post facto_ study intended to defend decisions that were not initially based upon cost. Under the stimulus of the statute, cost accounting has developed rapidly, and some companies have tried to maintain cost records suitable for use in setting their price differences; but the results have been disappointing.[82]

At the time that Section 2 (a) was amended, sellers whose price structures were illegal under the amended law often wanted to change them. Many of these sellers had reduced prices under pressure from certain buyers, but did not know enough about their costs to know how far their existing price differentials could be justified by cost differences. Recognizing the condition, the Commission did not immediately start enforcing the law by legal process. Instead, during an initial period of time it made a group of senior staff members, of whom I was one, available for talks with firms that wanted help in appraising their own prices, and it took no legal action if, as a result of such help, the prices were so revised as to be apparently lawful.

Most of the conferences focussed upon quantity discounts. They often ended in recognition that small differences in quantities had received no discount but discounts had been available for relatively large quantities and had become larger for still larger quantities; yet underlying differences in cost arose largely from the fact that there were lump-sum costs in making a sale, recording it, making delivery, and receiving payment, and these costs changed substantially per unit of product with small increases in quantity (that received no discount) but were trivial per unit for increases in quantities already large. After the talks, many firms voluntarily reduced or eliminated their discounts for large quantities, though few of them initiated discounts for increase in small quantities. These voluntary changes probably account for the fact that after enforcement of the law began the Commission's complaints, though they included various challenges to volume discounts, included very few about quantity discounts.

Section 2 (b) of the Act places upon the seller the burden of rebutting <u>prima facie</u> proof of price discrimination by showing cost justification. Such justifications have been submitted in relatively few of the cases in which the Commission has alleged violation of Section 2 (a). Presumably they have not been attempted in the other cases for several reasons: a) the respondent chose to dispose of the case quickly by not contesting the complaint; b) the task of cost justification was too costly to be worth attempting, or c) the kind of discrimination involved was one that could not be plausibly related to cost differences, e.g., it consisted of unsystematic price concessions to particular customers, or of grant of volume discounts to buyers that did not buy the specified volumes, or of similar kinds of off-scale selling, or of territorial price differences perversely related to differences in transportation expense. In some instances, a respondent offered cost justifi-

cation for only part of the alleged discrimination, and in some the Commission thought the justification valid for only part of the differences as to which it was submitted.

Recognizing the scarcity of suitable cost information and the difficulty of bringing it to relevant focus, both the Commission and the courts have been lenient in evaluating what was submitted. In one case, the Commission's opinion said, "Cost studies of the sort presented in this matter ordinarily do not afford precise accuracy but must necessarily embrace a number of conjectural factors and allocations. There is inherent in them a reasonable margin of allowable error. Where they are made in good faith and in accordance with sound accounting principles, they should be given very great weight .... Respondent's burden under the act is very great and it should have a liberal measure of consideration when it becomes apparent that it has made sincere and extensive efforts to discharge that burden."[83] In a private suit, the Second Circuit expressed itself similarly. As to averages submitted by one of the parties, it said: "To require a seller in these circumstances to justify the cost differential in each and every transaction with his buyers, rather than on the aggregate basis of their dealings, would prove unduly onerous. The impact of such a requirement might be to discourage <u>all</u> price differentials, even those actually justified by cost distinctions."[84] As to certain accounting improvisations in the case, it said: "Although such an accounting method obviously lacks the full measure of desired precision, it appears to have been undertaken in good faith and to accord with the minimal requirements of sound accounting principles .... Both the courts and the Federal Trade Commission have recognized the dilemma confronting defendants in suits such as these,

and have liberally accepted data derived from litigation-inspired accounting methods." One aspect of this leniency has been that the Commission disregards as de minimis slight residual price differences that remain unjustified by cost in situations in which the respondent has successfully justified most of the differences.[85]

A major problem in justification is to find acceptable groupings of products and buyers for purposes of cost comparison. Where the seller provides a long line of products, there is often no problem as to discrimination that probably would require a product-by-product comparison. In such cases, the Commission will authorize grouping of products in cost computation.[86] Grouping of buyers, however, is frequently important to the decision of the case. For cost computation, each class of buyers as to which costs are averaged must be reasonably homogeneous -- that is, it must include all buyers with whom transactions are similar in the way that they affect costs and must exclude all buyers with whom transactions are dissimilar in such ways. As the Supreme Court said in rejecting a cost defense by Borden in 1962: "A balance is struck by the use of classes for cost justification which are composed of members of such self-sameness as to make the averaging of the cost of dealing with the group a valid and reasonable indicium of the cost of dealing with any specific member. High on the list of 'musts' in the use of the average cost of customer groupings under the proviso of Section 2 (a) is a close resemblance of the individual members of each group on the essential point or points which determine the costs considered."[87]

Where a seller seeks to cost-justify low prices to a very small number of customers by

comparing his costs in sale to them with his costs in selling to all of his other customers as a group, his defense is likely to fail for lack of homogeneity; for some of those that do not get the low prices are likely to have characteristics that differentiate them from the others and make them similar to the favoured few.[88]

When buyers have been grouped into acceptable classes, problems remain as to types of cost that can be used in ascertaining cost differences. Where price differences must be justified for particular products that are only part of the maker's line of products, the first necessary step is to segregate the costs attributable to those products from the other costs. Often this involves substantial difficulties in apportionment of joint costs. If the method of apportionment that is used seems arbitrary or likely to enhance unduly the relevant costs and thereby enhance the relevant cost differences, this defect may invalidate the cost justification.[89]

If appropriate segregation of costs by commodities is achieved, the next step is segregation of costs by classes of buyers that pay different prices. Should the Commission challenge the price differences, each price to each class of buyer (if found to be injuriously different) will need to be cost-justified against each of the other prices. The larger the number of price classes, the more elaborate must be the segregation. More than once the Commission has accepted justification of some of a respondent's price differences but rejected it for others. In the light of the difficulties of segregating costs, firms have incentive to keep their price classes few. Offsetting this incentive, however, is the fact that the smaller the number of price classes the larger is the possibility that some of the buyers placed in the class will be so different from the others that the average cost attributed to the

class will be inappropriate to them.

Manufacturing costs seldom can be reasonably segregated by type of buyer. They may differ from buyer to buyer if goods are made to the buyer's specifications; or if production is intermittent and significant costs of resetting machines are necessary before each production run, and these costs can be spread over more units if the run is longer. Usually, however, production is a continuous process in which cost per unit of product is not affected by differences in transactions with particular buyers. Where this is so, the Commission and the courts will reject any effort by the seller to attribute to buyers that buy in large amounts a disproportionate part of any economies of scale in the manufacturing process that he attains by increase in his total business; for the total volume of business is derived not only from the few large purchases but also from the many small ones, and is not differentially attributable to either.

The relevant cost differences usually arise in distribution. Sales to different buyers often involve differences in methods of establishing contact, in extent and kind of sales effort, in amount of clerical work, in the location and duration of storage of goods, in transportation expense, in special services to the buyer, and in difficulties in obtaining payment. The Supreme Court indicated in a dictum in one decision that Section 2 (c) precludes allowances to buyers based upon difference in brokerage fees.[90] In all other respects the cost proviso of Section 2 (a) is broad enough to cover whatever differentials can be identified by cost accounting.

The problem of identification, however, is substantial. Some costs are not clearly traceable to particular sources, and some might be allocated in more than one reasonable way. The

Commission described the problem in 1941 in these terms: "... where the expenditure is of a joint nature ... an allocation must be made ... Often it is difficult to find the unit of effort or service which most uniformly represents the same amount of expenditure and for which statistical data are avoidable. For example, if it is desired to ascertain the direct selling cost of a commodity by customer classes all of which are served by the same salesman, shall salesman's selling effort be measured by the number of calls or by the number of minutes -- that is, by the call unit or by the time unit? Or may there, under the given conditions, be some other measuring unit more satisfactory? For which unit is it most practicable to obtain the necessary information and will that unit represent a uniform amount of expenditure? Regardless of the unit chosen, it frequently is necessary to make elaborate special studies to obtain this information."[91] The Commission thought the task harder for distribution costs than for manufacturing costs because a) distribution processes are less standardized; b) distribution costs normally have more classifications and types of analysis, e.g., by commodity, distribution channel, territory, quantity sold or delivered, and method of sale or delivery, and c) joint costs are more pervasive in distribution.

A firm that attempts cost justification must cope with such difficulties in such a manner that the results are plausibly reasonable and devoid of identifiable bias, and thus come within the limits of the leniency that the Commission and the courts show toward effort in good faith.

Few of the differences in cost are likely to be quantifiable by class of customer unless business records have been kept with such quantification in mind; and even where the records have been

suitably designed, use of them in justifying price differences requires in most cases special analysis. Moreover, some of the relevant costs may change significantly with change in the total size of the class of customers to which these costs are relevant and with adaptation of the seller's methods of sale and delivery to such changes in size. Thus the results of cost studies are likely to become obsolete with passing time.

Receipt of Unlawful Price Discrimination: Section 2 (f) provides "that it shall be unlawful for any person engaged in commerce, in the course of such commerce, knowingly to induce or receive a discrimination in price which is prohibited by this section."

This provision, apparently limited to price discrimination by an oversight due to congressional haste,[92] does not cover all discriminatory concessions. When the brokerage provision is violated, buyer as well as seller is a violator under Section 2 (c), discussed above. When a seller provides disproportionate allowances in violation of Section 2 (d), the buyer may be in violation under Section 2 (f), but only if the circumstances are such that the discriminatory allowances can be interpreted as indirect discriminations in price.[93] Otherwise, violations of both Sections 2 (d) and 2 (e) do not impose liability upon buyers. However, in coping with discriminatory allowances and services the Commission uses Section 5 of the Federal Trade Commission Act to impose liability upon buyers by interpreting their receipt of such favours as unfair methods of competition.[94]

But the clear meaning of Section 2 (f) is to establish buyer liability for price discrimination as Section 2 (a) establishes seller liability. What follows will pertain to this type of meaning.

Section 2 (f) is substantially more difficult to use than Section 2 (a). There are problems of interpretation of its commerce clause that have not yet been wholly removed.[95] Apart from these, the wording of the section clearly makes the buyer liable only if the seller is liable. That cases against buyers are thus dependent upon the illegality of conduct by others creates difficulty in developing such cases. A <u>prima facie</u> case against a seller can rest upon his conduct alone, and can be based upon examination of a substantial sample of that conduct. Such a case can become the basis for a broad order after examination of the seller's contentions about his own costs and the evidence that he produces about low prices by his competitors. In developing a case against a buyer, no such economy of effort is possible. If a powerful buyer gets discriminatory price reductions from several sellers, these are unlawful only in instances in which the seller acted illegally; and a showing that he did so requires that a series of possible cost justifications and justifications as to meeting competition be considered and found inadequate. Only by thus broadening the field in which illegality is found can the case against the buyer support an order broad enough to amend his general course of conduct.

Moreover, the buyer acts illegally only if he does so "knowingly." At first the Commission interpreted this word to mean that the buyer must be aware of the fact that there was a price differential. Using this interpretation, it obtained consent by several powerful buyers to orders against them.[96] But the interpretation was tested and rejected in the Automatic Canteen case.[97] The Supreme Court held (with three justices dissenting) that knowledge means guilty knowledge - that "the buyer whom Congress in the main sought to reach was the one who, knowing

full well that there was little likelihood of a defense for the seller, nevertheless proceeded to exert pressure for lower prices." It therefore required the Commission to show that the buyer "is not an unsuspecting recipient of prohibited discriminations." The requirement meant that the buyer must know not only that there is a price discrimination but also that it is large enough to be a source of injury.

The Court also changed the burden of proof about at least one and possibly both of the defenses available where there is injurious discrimination. In cases against sellers, the Commission had proceeded, in accord with Section 2 (b), to place upon the seller the burden of introducing and proving his cost defense; and the Commission had taken the same position in the case against Canteen. The Court held, however, that a buyer is not liable if the lower prices "are either within one of the seller's defenses such as cost justification or not known by him not to be within one of those defenses." The Court amplified as follows: "...we think the fact that the buyer does not have the required information, and for good reason should not be required to obtain it, has controlling importance ... Certainly the Commission with its broad power of investigation and subpoena, prior to the filing of a complaint, is on a better footing to obtain this information than the buyer."

Thus the Court imposed upon the Commission the burden of proving both that there was no valid cost defense and that the buyer had such information that he knew or should have known that this was true. Though the issue before the Court had to do with cost justification, the Court's language was broad enough that it might pertain also to the defense of meeting competition. However, elsewhere the decision remarked that since the buyer is likely to

know about prices that other buyers are paying, he would be well qualified to show the existence of another competitive offer at a low price if he desired to use such an offer in defense.

The decision included suggestion by the Court about how the Commission might cope with its duty to show the buyer's knowledge. It said that: "Trade experience in a particular situation can afford a sufficient degree of knowledge to provide a basis for prosecution ... The Commission need only show, to establish its prima facie case, that the buyer knew that the methods by which he was served and quantities in which he purchased were the same as in the case of his competitor. If the methods or quantities differ, the Commission must only show that such differences could not give rise to sufficient savings in the cost of manufacture, sale or delivery to justify the price differential, and that the buyer, knowing these were the only differences, should have known that they could not give rise to sufficient cost savings."

With its burden of proof thus enhanced, the Commission reconsidered what was pending before it and changed its methods of attack. For inability to prove enough knowledge by the buyer, it dismissed pending cases against Safeway Stores, Kroger, Philco, Sylvania Electric Products, and Crown Zellerbach. It continued to develop certain pending cases against buying groups concerned with automobile accessories. In subsequent proceedings in which it had no direct evidence about the knowledge of the buyer, it developed its case by showing the seller's costs and inferring that no reasonable man could have believed that the discounts the buyer received were cost-justified. Inferences of this kind obviously can be persuasive only where the gap between costs and prices is wide.

This procedure has been adequate as to discounts to buying groups where, apart from negotiations about discounts, there was no substantial difference between transactions by sellers with members of the group and with other buyers.[98] It failed, however, in a case in which the buyer, a cooperative of automobile parts dealers, used different buying methods and performed different services than the jobbers to whom the suppliers sold. In this case, the Commission's decision was reversed because it had not been based upon evidence showing that the difference did not reduce costs sufficiently to justify the lower prices.[99]

The Commission's attack under Section 2 (f) was also successful in a recent case that involved discounts for promotional services that the Commission challenged under both Sections 2 (f) and 2 (d). Here an appellate court held that the buyer's promotional activity gave him information enough that, possessing it, he should have inquired about promotional payments to other buyers.[100]

The Decline of Enforcement

Earlier parts of this chapter have contained indications that in various respects application of the Robinson-Patman Act has included, alongside corrective action that was an appropriate part of antitrust policy, instances of inconsistency difficult to avoid because of lack of clarity and consistency in the Act itself, and instances of application of the law that had dubious merit - intervention to protect buyers from harmless trade practices, protective interventions against slight or doubtful injury to groups of purchasers, and even proceedings that had anticompetitive impact. Though some of these results were attributable to defects in the statute and some to the fact that correction of inequities is likely to include proceedings that, though impor-

tant to persons mistreated, have no impact helpful in maintaining a viable competitive system, the development of such applications of the law soon aroused severe criticism of the Robinson-Patman Act both among those who had responsibility for enforcing it and in public discussion. Though both the Department of Justice and the Federal Trade Commission have jurisdiction to apply Section 2 of the Clayton Act as amended by the Robinson-Patman Act, and the Department of Justice alone has authority to proceed on the Government's behalf under the criminal provision of the amendatory act, the Department has done almost nothing to apply either part of this law. This inaction apparently has been due to adverse appraisal of the Act and of most proceedings under it. Within the Federal Trade Commission, some senior members of the staff also made adverse appraisals of parts of the Act and of many of the proceedings under it, particularly those concerned with brokerage and those concerned with the more dubious kinds of competitive injury. After amendment of the merger law in 1950, staff criticism tended to grow, for in comparison with the numerous instances in which merger law could be used to avert anticompetitive developments in particular markets and concentrative tendencies in the economy as a whole, remedial action against instances of price discrimination came to seem to many staff members and some members of the Commission itself to deserve a lower appraisal in establishing priorities. These internal developments were strengthened by criticism in learned journals, to the general effect that the Robinson-Patman Act fitted the general policy of the antitrust laws badly and that there might be doubt whether it had promoted more competition than it had retarded.

The culmination of criticism of the Robinson-Patman Act came in three documents in the late 1960's and early 1970's. Two task forces on antitrust policy appointed by two successive Presidents, though they differed as to many aspects of policy, were alike in that their reports included severe criticism of the Robinson-Patman Act. The first report said that the law had "discouraged types of price differentials which might have improved competition by lessening the rigidity of oligopolistic pricing or by encouraging new entry" and that "in numerous other respects" the Act had "injured competition."[101] The report said that the Act "requires a major overhaul," and included a suggested draft of a revised statute. The second report, even more severe in its criticism, advocated repeal of subsections (c), (d), and (e) and broadening of the defenses applicable to subsection (a), "so as to make them more readily available for sellers whose price differentials do not stem from a predotory purpose and do not injure competition in the market place (as opposed to disadvantaging individual firms)."[102] A third adverse criticism appeared in a report by a committee that the American Bar Association appointed to study the Federal Trade Commission.[103]

Commenting about these reports in a speech in May 1975, a Commissioner of the Federal Trade Commission said that "Robinson-Patman is being slowly anesthetized," argued that the Act "provides small firms with equality of opportunity and protection against unjustified differences in treatment" and said that its goals "are no less legitimate today than they were 39 years ago."[104]

The developing attitude in the Commission, which ranged from diminishing enthusiasm to adverse appraisal, resulted during the 1960's

in two types of change in the way that price discrimination problems were treated. One was effort to replace litigation by some kind of less formal action. In the 1950's action about price discrimination nearly always had consisted in formal complaint that ended in an order after contest, a consent order, or a dismissal. The first significant departure from this pattern was use of trade practice rules in the cosmetic industry as early as 1951 as a means of changing and making more flexible the Commission's previous interpretation of Section 2 (e) of the law.[105] In 1960 the Commission issued a pamphlet "guide" to the meaning of the law's provisions about allowances and services in Sections 2 (d) and 2 (e), and it has subsequently re-issued that guide in revised form.[106] During the 1960's, use of various kinds of non-litigative procedures developed rapidly, primarily because they were suited to the Commission's responsibilities as to advertising, labeling, and misrepresentation under various laws;[107] but these procedures came to be used as to price discrimination also.

As described in the Commission's annual report for 1968, these procedures were as follows: "Keeping in mind always the degree of public interest involved, cases were handled informally and on as broad a scale as practicable. If the problem was widespread and could be alleviated by clearer understanding of the law's requirements, the Commission would issue Industry Guides; if it appeared that guidance needed firmer backstopping, FTC promulgated Trade Regulation Rules upon which it could rely in the prosecution of cases; and if the Commission had reason to believe that law violations could be halted without recourse to time-consuming formal orders, it was willing to accept from individual respondents their formal assurances that the illegality would be discontinued. In addition, FTC issued Advisory

Opinions on the legality or illegality of proposed courses of action by individual businessmen or business groups. By all of these means, the Commission sought either to forestall violations or to curb them with the least expenditure of manpower. Even by thus lightening its case load, the Commission was confronted with more than enough hard-core violations capable of being halted only by formal orders."[108]

By 1965, use of such procedures had become established not only as to deceptive practices but also as to price discrimination. The Commission's annual report for that year spoke of "the increasingly obvious truth that more compliance with the law can be achieved by clearly defining its requirements and persuading businessmen to abandon illegal practices without the delay and cost of litigation than to strive for casework statistics," and of "illegalities of a character and scope that can be countered effectively by the issuance of Industry Guides, Trade Practice Rules, or Trade Regulation Rules."[109] It also emphasized the value of advisory opinions to particular businessmen. Prominent in such work have been revisions of the guide about allowances and services under Sections 2 (d) and 2 (e), inclusion of similar guidance in publications about particular industries such as those selling greeting cards and beauty and barber supplies, and provisions giving similar interpretations legal status in rules issued about men's and boys' tailored clothing.[110]

Apart from such broad developments, the Commission has supplemented its means of extralegal action by two devices concerned with particular violations: a) acceptance of "assurances of voluntary compliance" from individual violators as substitutes for formal complaints and formal orders, and b) informal "disposition" of so-called "informal cases," which apparently have been still less explicitly structured.[111]

In the years 1966-1970, assurances of compliance were used systematically, and in at least three of these years they were more numerous than formal orders.[112] Informal dispositions were still more numerous. Between 1966 and 1970 they apparently were several times the total of orders and assurances combined.[113]

With this change has come a second -- decrease in the importance attached to price discrimination as a part of the Commission's field of action. As early as the 1950's, the commission had begun to avoid what senior members of the staff regarded as over-emphasis upon brokerage cases.[114] During the 1960's the importance of various other kinds of price discrimination proceedings was down-graded. This was done informally and gradually, and has left no clear trace in public records. The trend was consolidated in 1970, when a broad structural reorganization included establishment of an Office of Policy Planning and Evaluation to "help the Commission establish its program and determine its priorities" and to "act as a counterforce to individual recommendations coming from various staff members interested primarily in only one area of the Commission's activity."[115] The duties of this Office include, in effect, exercise of veto power as to proposals that formal complaints be issued. Its influence appears to have been used against proposals for price discrimination proceedings.

Recently there have been few formal cases about price discrimination. In the fiscal year 1972, in which the Commission issued a total of 18 formal complaints, two of these charged violation of the price discrimination law, and one of the two included that charge with other charges. In that year the Commission issued 18 formal orders, of which three pertained to viola-

tion of Section 2 and one pertained to unlawful receipt of allowances. In the fiscal year 1974, the Commission issued 11 complaints, one of which - the only one that involved price discrimination - challenged under Section 5 of the Federal Trade Commission Act use of a basing-point system by plywood manufacturers. In that year, 24 cases ended in orders. Of these, nine pertained to price discrimination - one against discrimination that violated Section 2 (a), three against violations of Section 2 (d), and five dismissing complaints that had charged violation of the brokerage provision. In March 1975, the cases proceeding toward adjudication by the Commission totaled 41. Of these, none involved price discrimination alone, but two included charges of price discrimination with other charges.

Currently the Administration is preparing a bill that would substantially amend the price discrimination law, but neither its content nor a reliable summary of it is publicly available. In a recent speech to the Antitrust Section of the American Bar Association, a Deputy Attorney General said: "An Administration task force is in the final stages of preparing recommendations to the President concerning reform or repeal of the Robinson-Patman Act. That Act clearly discourages price competition and may operate to encourage vertical integration by large retailers."[116] In another recent public statement, an attorney of the Antitrust Division of the Department of Justice summarized official criticism of the Act as follows: "Unfortunately, the Robinson-Patman Act, while no doubt preventing the demise of some businesses in the short run, in many cases had hurt both the consumer and those it was supposed to preserve - the small entrepreneur. It has done this by reinforcing oligopoly pricing, by making entry against those with entrenched positions more difficult, and by preventing businesses, small

as well as large, from tailoring their pricing structure to reflect the demands of the market in which they do business. Indeed, the Robinson-Patman Act may in some instances have actually enhanced the position of large corporations by encouraging vertical integration and the use of private brands. On balance, we believe that supposed benefits of the Robinson-Patman Act have not justified the continuation of that statute's restrictions on entrepreneurial freedom in their present form."[117]

There is already indication that the bill will encounter substantial opposition by several organizations that speak on behalf of small business. A lively controversy about public policy toward price discrimination is imminent.

V - PRICE DISCRIMINATION

Footnotes

1. In its 1914 version, Section 2 read as follows: "It shall be unlawful for any person engaged in commerce, in the course of such commerce either directly or indirectly to discriminate in price between different purchasers of commodities, which commodities are sold for use, consumption, or resale within the United States ... where the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly in any line of commerce: Provided, that nothing herein contained shall prevent discrimination in price between purchasers of commodities on account of differences in the grade, quality, or quantity of the commodity sold, or that makes only due allowance for difference in the cost of selling or transportation, or discrimination in price in the same or different communities made in good faith to meet competition: and provided further, that nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandises in commerce from selecting their own customers in bona fide transactions and not in restraint of trade."

2. For citations to these cases, see Corwin D. Edwards, The Price Discrimination Law, Brookings Institution, Washington, D.C., 1959, p. 6.

3. Ibid, p.6.

4. The earlier decision was in Mennen Co. v.

F.T.C., 288 F. 774 (1923); the latter in George Van Camp & Sons Co. v. American Can Co., *et. al*., 278 US 245 (1929).

Between 1919 and 1927, sales by chain groceries almost quadrupled; sales by chains of variety stores, drugstores, and candy stores more than doubled, and there were lesser substantial increases by chain tobacconists, chain shoe stores, wearing apparel chains, and chains of retail outlets for mail order houses. See Bureau of the Census, *Statistical Abstract of the United States*, 1928, p. 325, and R. M. Clewett (ed.), *Marketing Channels for Manufactured Products*, 1954.

Among these were a) discriminatory state taxes (enacted in several states) computed at a rate per store that was graduated upward with increase in the total number of outlets possessed by the chain nationally; b) state laws (enacted by several states) against sale below "cost", devised as a preventative against use of "loss leaders"; c) state laws (enacted by most states) authorizing resale price maintenance for branded goods, with amendment of the Sherman Act and the Federal Trade Commission Act to exempt restraints upon interstate commerce incident to such laws, and d) pressure, as noted below, for revision of the law of price discrimination.

The instruction by the Senate appears in Senate Resolution 224, 70th Congress, 1st session (1926). The reports were summarized by the Commission in its annual report for 1935, pp. 32-40.

8. U.S. v. Bowman Dairy Co., 89 F. Supp. 112 (N.D. Ill, 1949).

9. U.S. v. National Dairy Products Corp., 372 US 29 (1963).

10. Nashville Mills Co. v. Carnation Co., 355 US 373 (1958). A previous decision by the Supreme Court in favour of the plaintiff in Moore v. Mead's Fine Bread Co., 348 US 115 (1954), had been rendered in a case in which he had sued under both Section 2 (a) of the Clayton Act and Section 3 of the Robinson-Patman Act, and the Court had not made a distinction between the two statutes.

11. The quoted phrases are from House Report 2287, 74th Congress, 2nd session. Similar language appeared in Senate Report 1502.

12. The quoted remark and others appear in Federal Trade Commission, Robinson-Patman Act, Congressional Expressions and Formal Decisions, February 1942.

13. For the process by which the Robinson-Patman Act became law, see Edwards, The Price Discrimination Law, op. cit., note 2, pp. 8-12 and 21-53, and Earl W. Kintner, A Robinson-Patman Primer, Macmillan, New York, 1970, pp. 10-16.

14. Section 2 (c) says "that it shall be unlawful for any person engaged in commerce, in the course of such commerce, to pay or grant, or to receive or accept, anything of value as a commission, brokerage, or other compensation, or any allowance or discount in lieu thereof, except for services rendered in connection with the sale or purchase of goods, wares, or merchandise, either to the other

party to such transaction or to an agent, representative, or other intermediary therein where such intermediary is acting in fact for or on behalf, or is subject to the direct or indirect control, of any party to such transaction other than the person by whom such compensation is so granted or paid."

15. The question arose before, and was uniformly settled in the same way by the Second, Third, Fourth, and Fifth Circuits in Biddle Purchasing Co., 96 F. 2d. 687 (2nd circuit, 1938); Oliver Brothers, 102 F. 2d. 763 (4th Circuit, 1939); Great Atlantic and Pacific Tea Co., 106 F. 2d. 667 (3rd Circuit, 1938); Webb-Crawford Co., 109 F. 2d. 268 (5th Circuit, 1940); and Southgate Brokerage Co., 150 F. 2d. 607 (4th Circuit, 1945).

16. This issue was raised not only in the five cases listed in note 15 but also in Quality Bakers of America, 114 F. 2d. 393 (1st Circuit, 1940), Modern Marketing Service, 149 F. 2d. 970 (7th Circuit, 1945), and Independent Grocers Alliance Distributing Co., 203 F. 2d. 941, (7th Circuit, 1953). Thus the same conclusion was reached in the First, Second, Third, Fourth, Fifth, and Seventh Circuits. In the Webb-Crawford case the court justified its conclusion by so changing the location of a comma as to alter the apparent meaning of the provision, and said, "Commas are not to be suffered to defeat the legislative meaning." In the Modern Marketing decision, the court said "...we think the proof shows that such services were genuine and of benefit to such sellers ... We are of the view that where such relationship exists it is immaterial whether the services

rendered the seller were genuine or fictitious and whether they were incidental or otherwise. Even good faith on the part of both the broker and the seller cannot be utilized to escape the condemnation of the provision."

17. Until 1960, the courts had rejected interpretations of price concessions as in lieu of brokerage only in two cases: one in which failure of proof was found in a proceeding for criminal contempt (in re. Whitney & Co., 273 F. 2d. 211, (9th Circuit, 1959)), and one in which a manufacturer had entirely ceased to use brokers and thereafter had reduced his prices (Robinson v. Stanley Home Products Co., 272 F. 2d. 601, (1st Circuit, 1959)).

18. Main Fish Co., 53 FTC 88 (1956).

19. Great A. & P. Tea Co., op. cit., note 15.

20. The A. & P. proceeding and what followed are summarized in Edwards, The Price Discrimination Law, op. cit., note 2, pp. 102-103, 107-111.

21. Illustrations are cases involving Quality Bakers, 114 F. 2d. 393 (1st Circuit, 1940); Modern Marketing Service, 149 F. 2d. 970 (1st Circuit, 1945); and Independent Grocers Alliance, 203 F. 2d. 941 (7th Circuit, 1953).

22. Examples are Biddle Purchasing Co., 96 F. 2d. 687 (2nd Circuit, 1938) and Oliver Brothers, 102 F. 2d. 763 (4th Circuit, 1939).

23. Examples are cases against Webb-Crawford Co., 109 F. 2d. 268 (5th Circuit, 1940): and Reeves-Parvin, 28 FTC 1429 (1939), Mississippi Sales Co., 30 FTC 1282 (1940), and Thomas Page Mill 33 FTC 1437 (1941). The latter three were not appealed.

24. Examples are cases against Southgate Brokerage Co., 150 F. 2d. 607 (4th Circuit, 1945), Fruit and Produce Exchange, 30 FTC 224 (1939), Custom House Packing Corp., 43 FTC 164 (1946), Columbia River Packers Association, 44 FTC 118 (1947), and Ketchikan Packing Co., 44 FTC 158, (1947). The latter three were not appealed.

25. Examples are Jack Herzog & Co., 150 F. 2d. 450 (2nd Circuit, 1945), Harry M. Bitterman, Inc., 35 FTC 49 (1942), and Joseph W. Efrid, 40 (FTC 373 (1945). The last two cases were not appealed.

26. Edwards, The Price Discrimination Law, op. cit., note 2, pp. 114-130.

27. Ibid., pp. 131-135.

28. Ibid., pp. 135-140.

29. Ibid., pp. 140-147.

30. Ibid.,pp. 147-150.

31. F.T.C. v. Henry Broch & Co., 363 US 166 (1960). The minority of the Court went further. It thought that the law does not cover "legitimately negotiated rates of commission for brokers' services;" that the provision is not applicable to "any" case concerned with the amount that a principal

pays his agent, and that the majority decision, by freezing brokerage rates, was anticompetitive.

32. Thomasville Chair Co. v. F.T.C., 306 F. 2d. 541 (5th Circuit, 1962). See also comments in Kintner, op. cit., note 13, pp. 213-215 and 225-226.

33. Central Retailer-owned Grocers, Inc. v. F.T.C., 319 F. 2d. 410 (7th Circuit, 1963). The Commission's decision appears in National Retailer-owned Grocers, Inc., 60 FTC 1208 (1962).

34. Empire Rayon Yarn Co. v. American Viscose Corp., 364 F. 2d. 491 (2nd Circuit, 1965), certiorari denied, 385 US 1002 (1967). See also the superceded decision, 354 F. 2d. 182 (2nd Circuit, 1965).

35. Docket 8066, Hruby Distributing Co., 61 FTC 1437 (1962). The revised version of the decision emphasized evidentiary problems in the case and ignored the minority's emphasis upon inconsistency between the decision and that in the Southgate case (150 F. 2d. 607). It said that the discounts were not proved to be brokerage.

36. See Western Fruit Growers Sales Co. v. F.T.C., 322 F. 2d. 67 (9th Circuit, 1963); Docket 8564, Garrett-Holmes Co., 67 FTC 237 (1965). See also Section 74.2 as to prohibited brokerage in the Commission's Trade Practice Rules for the Fresh Fruit and Vegetable Industry.

37. Section 2 (d) requires that the payments be made in the course of commerce; Section 2 (e) contains no such requirement. Section 2 (d) pertains to proportionality among competing customers; Section 2 (e) pertains to "all purchasers"; and Section 2 (b), which provides that a prima facie case can be rebutted by showing that offers by competitors were met in good faith, speaks of furnishing services and facilities, but not of payments for service. For a time this kind of rebuttal was accepted as to Section 2 (e) but not as to Section 2 (d), but in the Exquisite Form Brassiere case (301 F. 2d. 499 (D.C. Circuit, 1961)),it was accepted as to Section 2 (d) also.

38. The development became apparent in the 1950's and soon resulted in a substantial change in the nature of proceedings under Section 2. In the period June 1953 - March 1957, cases instituted by the Commission under Section 2 (d) and 2 (e), which had been infrequent before, became the most frequent types of discrimination case. See Edwards, op. cit., note 2, pp. 69-70 and 170-172.

39. In the 1950's, 11 cases were instituted by the Commission against provision of advertising allowances to two regional chains, and of these, 10 resulted in orders, though one was set aside on appeal for reasons irrelevant to this note. The chains, at whose initiative the allowances had been made, were charged with violation of Section 5. Subsequently, similar proceedings under Section 5 became common. See Edwards, op. cit., note 2, p. 165.

40. For discussion of other possible meanings see Edwards, op. cit., note 2, pp. 156-164. For disposition of a private suit in which defendants offered a different interpretation, see State Wholesale Grocers v. Great Atlantic and Pacific Tea Co., 258 F. 2d. 831 (7th Circuit, 1958), certiorari denied, 358 US 947 (1959).

41. Fred Meyer, Inc. v. F.T.C., 390 US 351 (1968). In this case the Commission's complaint included both Section 5 and Section 2 (f), and the circuit court (359 F. 2d. 351, 9th Circuit (1966)) sustained the order under Section 2 (f) by holding that the promotional allowance that had been challenged, which included receipt of rebates from suppliers, was an indirect discrimination in price. Though this decision, if followed, gives the Commission an additional means of proceeding against buyers in some instances of violation of Section 2 (d) by sellers, the difficulties involved in use of Section 2 (f) (see below) probably are great enough to make use of Section 5 the preferable course.

42. This interpretation was applied only after the Commission had tried a different one. The Elizabeth Arden case pertained to a producer of cosmetics that provided demonstrators to assist retailers. Demonstrators were provided by Arden to 265 of about 3,000 retailers that sold Arden products; these 265 accounted for about 40 per cent of Arden's total sales. Though demonstrators could be useful only in stores that had enough space for them and enough business to keep them occupied, the Commission's order, brushing aside these difficulties, said that if Arden chose to use demonstrators they must be

provided proportionately. The decision was affirmed on appeal. See Elizabeth Arden, Inc. 39 FTC 288 (1944), affirmed 156 F. 2d. 132 (2nd Circuit, 1946), certiorari denied, 331 US 806 (1947). The decision aroused protest. Manufacturers saw no practical way of making demonstrators generally available; large retailers wanted the services continued; small retailers saw no use in the tiny demonstration services to which they would be entitled. By 1951, the Commission had decided that the previous interpretation was "narrow and impracticable." With two dissents, it approved trade practice rules for the cosmetic industry which contained a reinterpretation. These said that if what was offered was not suitable to the business of some recipients of the offer, the law's requirement could be met by offering these customers suitable alternatives of "equivalent measureable cost." See Federal Trade Commission, <u>Trade Practice Rules for the Cosmetic and Toilet Preparations Industry</u>, November 29, 1951. See also discussion in Edwards, <u>op</u>. <u>cit</u>., note 2, pp. 195-200.

43. Federal Trade Commission, <u>Guides for Advertising Allowances and Other Merchandising Payments and Services</u>. Promulgated May 29, 1969, as amended August 4, 1972. An earlier version of the guide was issued in 1960.

44. In Vanity Fair Paper Mills, Inc. v. F.T.C., 311 F. 2d. 480 (2nd Circuit, 1962) the Second Circuit held that an allowance is not available if the provider of it has tried to conceal its existence from a competing customer. Vanity Fair's offense

had been to grant to one distributor a larger promotional allowance than that offered in its standard contract without telling its other customers that this was available to them also. The fact that these customers did not actually get the allowance was considered enough to shift to Vanity Fair the burden of proving that they knew that it was available to them.

45. The Commission asserted in the General Foods case the seller's duty to preserve a "discernible relationship between the amount paid and the cost or reasonable value of the services rendered." (General Foods Co., 52 FTC 798 (1956)). The published guide says that the seller should take "reasonable precautions to see that services he is paying for are furnished and also that he is not overpaying for them." See Guides, op. cit., note 43.

46. In work upon my book on price discrimination in the late 1950's, I found instances in which particular large distributors obtained in aggregate advertising allowances as much as 20 per cent, 25 per cent, and even 50 per cent of large advertising budgets, apparently without need to modify the advertising programs that they would otherwise have adopted in order to get the allowances. See Edwards, op. cit., note 2, pp. 205-206.

47. See Edwards, op. cit., note 2, pp. 181-183. The decision appears in 51 FTC 89 (1954).

48. Ibid., p. 185. The decision appears in 39 FTC 82 (1944).

49. A proviso in Section 2 (a) says that: "Nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandise in commerce from selecting their own customers in bona fide transactions and not in restraint of trade." In the light of this provision, the Commission held as early as 1937 that the seller "may discriminate in the choice of customers" (Baird & Sons, Inc., 25 FTC 548), and the Third Circuit held in 1939 that the term "purchaser" does not include one who wishes to purchase (Shaw's Inc. v. Wilson-Jones Co., 105 F. 2d. 331).

50. Though the concept of prevention has been applied, it has never been literally interpreted. Applied to wholesale discounts, for example, its literal meaning might be that retailers are injured because denial of such discounts to them prevents them from competing at the wholesale level. As actually used, the concept of prevention covers only prevention of competition at the same horizontal level as is occupied by the buyer.

51. Since discrimination often involves sale to different buyers at different times, the authorization to change prices though time can involve difficult problems of interpretation. In the Atalanta case (Atalanta Trading Corp. v. F.T.C., 258 F. 2d. 365 (1958)), the Second Circuit set aside an order based on isolated non-recurring transactions five months apart, saying, "the time interval is a determining factor." In the Fred Meyer

case, however (Fred Meyer, Inc. v. F.T.C., op. cit., note 41), the Ninth Circuit thought that a time interval of several months did not exempt transactions in a standardized commodity sold widely and frequently. Relevant variables include substantial changes in supply or demand, the commodity's durability, and changes in style, design, or technological characteristics.

52. Differences in the grade and quality of peaches picked and packed in different places were considered inadequate, since sales invoices described the peaches identically. See Fred Meyer, op. cit., note 41. The court held that "commercial fungibility ... is all the Robinson-Patman Act demands."

53. See for example, Docket 3624, Hansen Inoculator, 26 FTC 303 (1938); Docket 4972, U.S. Rubber Co., 46 FTC 998 (1950); Docket 5722, Whitaker Cable Corp. 51 FTC 958 (1955).

54. Docket 7129, Borden Co., 1963; set aside 339 F. 2d. 953 (7th Circuit, 1964); reversed 383 US 637 (1966). In the Supreme Court two justices dissented, and noted that when the Commission considered a respondent's defense that he had met competition in good faith it did not regard that defense as sufficient to cover reduction of the price of a premium brand to the level of a competitor's price for a non-premium brand.

55. In the Bausch & Lomb case (Docket 3233, Bausch & Lomb Optical Co., et. al., 28 FTC 186 (1939)) and the American Optical Company case (Docket 3232, 28 FTC 169 (1939)), the Commission found

that discrimination by each of two large competing makers of optical goods tended toward monopoly by that company. In other cases, tendency toward monopoly was imputed to discrimination by one small firm but not to a similar competitor. Krengel and Moss, for example, were makers of rubber stamps. Moss had about 19 employees, Krengel about 10. Both sold at prices that differed widely from buyer to buyer in ways apparently not related to amounts bought. Their prices had diverted some buyers to them from other producers; and one competitor of Moss had ceased selling stamps. In both cases, the Commission found the narrow kind of injury. In the Moss case, in spite of the fact that there were more than 70 makers of stamps in New York City alone, it also found the broad type of injury and a tendency to create a monopoly. See Docket 4405, Samuel H. Moss, 36 FTC 648 (1943) and Docket 5516, Krengel Manufacturing Co., Inc., 46 FTC 80 (1949). See also Edwards, op. cit., note 2, pp. 477-482.

56. This provision is qualified by a proviso that the Commission, after investigation and hearing, may fix quantity limits for commodities "where it finds that available purchasers in greater quantities are so few as to render differentials on account thereof unjustly discriminatory or promotive of monopoly in any line of commerce"; and that thereafter differentials for greater quantities shall not be permitted. The Commission has made only one effort to fix much a limit. After investigation of the tire industry it promulgated in 1949 a quantity limit of one carload for replacement tires. Numerous

objections to the rule reached the Court of Appeals for the District of Columbia, were consolidated there into a single case which was remanded to the district court for judgment on the merits, and there resulted in a declaratory judgment against the rule, which was then affirmed by the court of appeals. (See F.T.C. v. B.F. Goodrich Co., et. al., 242 F. 2d. 31 (1957)). The Commission did not appeal the case further. This chapter will say no more about the proviso.

57. Docket 4389, Standard Oil Co., 173 F. 2d. 210 (1949); 340 US 231 (1951).

58. In a private suit (Perkins v. Standard Oil of California, 395 US 642, (1969)),the Supreme Court held in 1969 that, "We find no basis in the language or purpose of the Act for immunizing Standard's price discriminations simply because the product in question passed through an additional formal exchange before reaching the level of Perkins' actual competitor." The decision reinstated a jury verdict that awarded damages to Perkins.

59. F.T.C. v. Morton Salt Co., 334 US 37 (1948).

60. Docket 5723, Moog Industries, Inc., 51 FTC 939 (1955); affirmed, Moog Industries v. FTC, 238 F. 2d. 43 (8th Circuit, 1956).

61. See Edwards, op. cit., note 2, pp. 366-379, 405-407, 412-417.

62. Joseph E. Sheehy, director, Bureau of Litigation, "Area Price Discrimination", before the

Association of General Counsel, Cleveland, Ohio, Oct. 23, 1957; quoted in Edwards, *op. cit.*, note 2, p. 452.

63. Docket 4556, The Curtiss Candy Co., 44 FTC 237 (1947), modified 48 FTC 161 (1951).

64. Docket 4389, Standard Oil Company., 41 FTC 263 (1945), modified 43 FTC 56. For decision by the Seventh Circuit in 1949 see 173 F. 2d. 210; for the Supreme Court decision in 1951 see 340 US 231. On remand the Commission rejected Standard's defense of meeting competition (see 49 FTC 923 (1953)), and the Seventh Circuit reversed (see 233 F. 2d. 649 (1956)).

65. 173 F. 2d. 210 (7th Circuit, 1949) at 217.

66. In the Anheuser-Busch case (Anheuser-Busch, Inc., v. F.T.C., 289 F. 2d. 835 (1961)), the Seventh Circuit said that where the discriminator is engaged in predatory action or buccaneering "a reasonable probability may be inferred that its willful misconduct may substantially lessen, injure, destroy or prevent competition." Predatory action influenced the decision in Utah Pie Co. v. Continental Baking Co., 386 US 685 (1967). See Kintner, *op. cit.*, note 13, pp. 114-119. Other relevant cases include E. B. Muller v. F.T.C., 142 F. 2d. 511 (6th Circuit, 1944); Moore v. Mead's Fine Bread, 348 US 115 (1954); Atlas Building Products v. Diamond Block & Gravel Co., 269 F. 2d. 950 (10th Circuit, 1959), certiorari denied, 363 US 843 (1960); Lloyd A. Fry Roofing Co. v. F.T.C., 371 F. 2d. 277 (7th Circuit, 1966).

67. In Docket 6018, General Foods, 50 FTC 887 (1956), the Commission's opinion said, "We do not believe the law makes the distinction between competitive injury to sellers and competitive injury to their customers that the above statement would seem to indicate ... The standard for determining the unlawfulness of an unjustified price discrimination, namely, the substantiality of the effects reasonably probable, is the same whether the competitive injury occurs at the seller level or at the customer level ... Under differing circumstances the proof necessary to establish injury or even to make out a prima facie case will differ."

68. Docket 4920, Minneapolis-Honeywell Regulator Co., 44 FTC 351 (1948).

69. Docket 8032, Dean Milk Co., 68 FTC 710 (1965).

70. Dean Milk Co. v. F.T.C., 395 F. 2d. 696 (7th Circuit, 1968).

71. Anheuser-Busch, Inc. v. F.T.C., op. cit., note 66. In Minneapolis-Honeywell Regulator Co. v. F.T.C., 191 F. 2d. 786 (7th Circuit, 1951), the same court had rejected the Commission's decision against Minneapolis-Honeywell on the ground that, even if the company had diverted business from competitors, the fact that these firms had been able to thrive was evidence that the price discrimination had not injured competition.

72. Balian Ice Cream Co. v. Arden Farms Co., 231 F. 2d. 356, (9th Circuit, 1955), certiorari denied, 350 US 991 (1966).

73. Standard Oil Co., _op. cit_., note 64. Meeting competition as an aspect of this case is discussed in Edwards, _op. cit_., note 2, pp. 319-328.

74. The Commission at first held that the defense fails if the reduced prices not only retain existing customers but also get new ones; but this view has been rejected on appeal. See Sunshine Biscuit, Inc. v. F.T.C., 306 F. 2d. 48 (7th Circuit, 1962).

75. In Viviano Macaroni Co. v. F.T.C., 411 F. 2d. 255 (3rd Circuit, 1969), the defense was rejected because Viviano had made no adequate effort to find out how much reduction of price would actually meet competitors' prices.

76. The Supreme Court rejected the claim that one may meet a seller's unlawful prices in the Staley case (324 US 746 (1945)), and took the same position for granted in its two opinions in the Standard Oil case (338 US 865 (1949), and 349 US 231 (1951)).

77. F.T.C. v. Standard Brands, Inc., 189 F. 2d. 510 (2nd Circuit, 1951). Standard had met competitors' prices for particular quantities but had applied those prices to smaller quantitites also.

78. _Ibid_. See also 46 FTC 1485, at 1495.

79. The point was emphasized by the Supreme Court in the Staley case (326 US 746 (1945)) in a situation in which Staley was adhering to a basing-point system. Twenty years later, in accepting a claim of meeting competition by Callaway Mills, an appellate court held that a carpet maker need not meet competition "in

a wholly piecemeal fashion," but could establish a system of volume discounts that, for comparable qualities, met the prices per yard customarily charged by its competitors, who had long used schedules of volume discounts. See Callaway Mills Co. v. F.T.C., 362 F. 2d. 435 (5th Circuit, 1966).

80. Congressional Record, Vol. 80, part 9, 74th Congress, 2nd session, p. 9417.

81. In 1946 a government price official reported to a congressional committee that probably 85 per cent of all industrial companies, with a total of about 75 per cent of all industrial production, did not allocate cost information on a product basis. See Office of Price Administration, A Report on Cost Accounting in Industry, June 30, 1946, p. iii.

82. In the 1950's the Commission appointed an advisory committee of outside experts on cost justification. This committee reported in 1956 that solution of cost problems raised under the Act demanded a degree of detail and continuity of records greater than that needed generally for good management. In the same year, the committee's chairman wrote, "Few laymen (in the accounting sense) are so unsophisticated as to believe that an economically feasible record-keeping system can be devised which would give an immediate answer to every Robinson-Patman problem. The experience of American Can Co., which actually carried out an ambitious project of this sort for nearly five years, does little to encourage emulation." See Herbert Taggart, "Cost Justification under the

Robinson-Patman Act," _Journal of Accountancy_, June 1956, pp. 52-56.

83. Docket 4920, Minneapolis-Honeywell Regulator Co., _op. cit._, note 68, at 394.

84. Reed v. Harper, 235 F. 2d. 420 (2nd Circuit, 1956), at 425.

85. Docket 4972, United States Rubber Co., decision, 46 FTC 998 (1950).

86. Docket 5728, Sylvania Electric Products Co., 51 FTC 282 (1955).

87. U.S. v. Borden Co., 370 US 460 (1962), at 469.

88. Such lack of homogeneity was important in rejection of cost defenses not only in the Borden case mentioned in note 87, but also in other cases. See American Can Co. v. Russellville Canning Co., 191 F. 2d. 38 (8th Circuit, 1951); Docket 3977, Champion Spark Plug Co., 50 FTC 30 (1953).

89. Standard Brands, for example, attempted to justify price differences upon bakers' yeast by a process that included division of its costs between grocery products and bakery products, followed by division of the latter between yeast and other bakery products. Use of arbitrary methods of division at these levels was one of the reasons for rejection of the cost defense. See Docket 2986, Standard Brands, Inc., 29 FTC 121 (1939); modified 30 FTC 1117 (1940).

90. F.T.C. v. Henry Broch & Co., 363 US 166 (1960).

91. F.T.C., Case Studies in Distribution Cost Accounting for Manufacturing and Wholesaling, 1941, pp. 28-30.

92. The relevant legislative history is summarized in Kintner, op. cit., note 13, p. 262.

93. See note 41 above.

94. Grand Union Co. v. F.T.C., 300 F. 2d. 92 (2nd Circuit, 1962); R.H. Macy & Co. v. F.T.C., 326 F. 2d. 445 (2nd Circuit, 1964); Fred Meyer v. F.T.C., op. cit., note 41.

95. Kintner, op. cit., note 13, p. 253.

96. Docket 3820, A.S. Aloe Co., 34 FTC 363 (1941); Docket 5027, Associated Merchandising Corp., 40 FTC 578 (1945); Docket 5794, Atlas Supply Co., et. al., 48 FTC 53 (1951).

97. Automatic Canteen Co. of America v. F.T.C., 346 US 61 (1953).

98. American Motor Specialties Co. v. F.T.C., 278 F. 2d. 225 (2nd Circuit, 1960), certiorari, denied 364 US 884 (1960); Mid-South Distributors v. F.T.C., 287 F. 2d. 512 (5th Circuit, 1961), certiorari denied 368 US 838 (1961).

99. Alhambra Motor Parts v. F.T.C., 309 F. 2d. 213 (9th Circuit, 1962).

100. Fred Meyer v. F.T.C., 359 F. 2d. 351 (9th Circuit, 1966). The Supreme Court reversed this decision, but on other grounds (390 US 341, 1968).

101. 1968 White House Task Force Report on Antitrust Policy (the Neal report), 115 Congressional Record 5651 (daily edition), May 27, 1969.

102. White House Task Force Report on Productivity and Competition (the Stigler report), 115 Congressional Record 647 (daily edition), June 16, 1969.

103. American Bar Association, Report of the ABA Commission to Study the Federal Trade Commission, Sept. 15, 1969. pp. 67-68, 99-101.

104. "Robinson-Patman is not Dead - Merely Dormant," address by Paul Rand Dixon, Commissioner, Federal Trade Commission, before Sales Promotion Conference, National Retail Merchants Association, Hollywood, Florida, May 21, 1975 (duplicated).

105. See note 42 above. One long-standing type of action in the Commission had been holding trade practice conferences from which emerged certain interpretations of the law and of wise business policy under the conditions of a particular industry. These "rules" were interpretations by the Commission after discussion with the industry, but had no legal validity except as predictions of the probable subsequent content of formal complaints and orders. They were thought useful in obtaining voluntary compliance. Traditionally the Commission had refused to use such rules

as to restraints of trade, including price discrimination, except by including in them paraphrases of the language of the statute itself.

106. See note 43 above and relevant text.

107. By the early 1970's, the Commission had responsibilities about such matters not only under the Federal Trade Commission Act but also under the Wool Products Labeling Act, the Textile Fiber Products Identification Act, the Fur Products Labeling Act, the Flammable Fabrics Act, the Fair Packaging and Labeling Act, the Truth in Lending Act, and the Cigarette Labeling and Advertising Act.

108. Federal Trade Commission, Annual Report, 1968, pp. 2-3.

109. Federal Trade Commission, Annual Report, 1965, p. 2.

110. The Federal Trade Commission Act gives the commission rule-making power. In the 1960's it began to use this power. A trade regulation rule is issued after due process of law, can be challenged in the courts, and, if it survives challenge, is an authoritative statement of law capable of being violated and enforced. Such rules are distinguished from "trade practice rules," which have existed over a longer period but which interpret law in ways that, though indicative of the Commission's opinion, have been formulated by consultation devoid of opportunity for formal contest and acquire legal validity only if and so far as

they are the basis for later orders that can be contested and appealed.

111. The so-called "informal cases" appear to be instances in which contacts about price discrimination by letter, personal interview, or telephone, between members of the Commission's staff and representatives of firms result in advice that something that the firm is doing or about to do is legally vulnerable and in statement by the firm's spokesman that the action in question will be abandoned or modified to avoid illegality. Such a statement differs from an assurance of compliance in that it is not reduced to writting nor formally signed on behalf of the firm. The figures about such cases do not distinguish acts that are clearly violations of law from acts that have merely dubious aspects, and possibly they include instances in which, after closer examination, the matter was closed because the act was lawful.

112. The annual report for the fiscal year 1968 did not give the information needed for this comparison. For the other fiscal years, the record was as follows: 1966, 74 orders, 39 assurances; 1967, 14 orders, 50 assurances; 1969, 10 orders, 15 assurances; 1970, seven orders, 21 assurances. See FTC annual reports: for 1966, p. 24; for 1967, p. 22; for 1969, p. 24; for 1970, p. 18.

113. The annual reports give the figures as follows: in 1966, initiated 81, disposed of 375, pending at close of year 318; in 1967, initiated 159, disposed of 165, pending at close of year, 310; in 1969,

initiated 53, disposed of 120, pending at close of year 241; in 1970, initiated 36, disposed of 178, pending at close of year 91. Pages in the reports are the same as for note 112.

114. Violations of Section 2 (c) reached their peak in the period September 1940 to June 1947, during which they constituted 75 per cent of all price discrimination orders. By the period June 1953 to March 1957, they were down to slightly less than 32 per cent. (See Edwards, op. cit., note 2, pp. 69-70.) In the early 1950's, I participated in a staff conference that decided against further proceedings against unlawful brokerage in a particular industry because a) analogous practices were thought to be prevalent there and working no discernible harm, b) to take action against only a few of them would be discriminatory, and c) to take action against all of them would be to use staff resources that were needed for cases that seemed more important.

115. Federal Trade Commission, Annual Report, 1970, p. 2.

116. Address by Harold R. Tyler, Jr., deputy Attorney General, before the Antitrust Section of the American Bar Association, Chateau Champlain, Montreal, Canada, August 12, 1975, (duplicated), p. 12.

117. Testimony of Joe Sims, special assistant to the Assistant Attorney General, Antitrust Division, before the Subcommittee on Activities of Regulatory Agencies of

the Committee on Small Business of the House of Representatives, July 10, 1975 (duplicated), pp. 10-11. The criticisms quoted are elaborated in the rest of this testimony.

V1 - INTERLOCKING DIRECTORATES

Provisions that curb interlocking directorates were included in Section 8 of the Clayton Act in 1914. The major part of them pertained explicitly to links among financial institutions, as parts of the regulation of banking.[1] These will not be discussed here. One part, however, was generally applicable to other links among large enterprises. Without subsequent change, it has remained in the statute. It provides that:

> ... no person at the same time shall be a director in any two or more corporations, any one of which has capital, surplus, and undivided profits aggregating more than $1,000,000, engaged in whole or in part in commerce, other than banks, banking associations, trust companies, and common carriers subject to the act to regulate commerce approved February 4, 1887, if such corporations are or shall have been theretofore, by virtue of their business and location or operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of the antitrust laws...

In enacting this provision, the Congress apparently intended to prevent the larger business corporations from using personal interlocks to evade the prohibition that Section 1 of the Sherman Act imposes upon restrictive agreements among competitors.[2] However, the provision is so limited that it does not clearly cover as to the larger corporations subject to it, all that this Section of the Sherman Act forbids to them. The Sherman Act is applicable to all agreements to restrain trade, whether horizontal or vertical,

whereas the law of interlocking directorates is applicable only to corporations that are large and are competitors. Thus this law is intended to be only a fragment of what would have been appropriate to a full effort to block use of personal interlocks as a means of evasion. Moreover, the enactment left open various types of linkage among competitors that the law did not cover.

The interlocks that are covered by this part of Section 8 are forbidden outright, whether or not they involve parts of the corporate boards large enough to give the identical directors decisive influence, and whether or not there is evidence that the interlocks have been used restrictively or that the interlocking directors intend so to use them. Since identity of directors appears clearly in corporate records and the size of the owners' equity in the relevant corporations can be ascertained from the corporate books or appears in the corporate balance sheets, and since in most instances competition between corporations that actually compete is not hard to prove, legal proceedings that result in complaint are not likely to result in acquittal. For this reason, most investigations under this part of Section 8 have brought about either resignations by any directors that held illegally interlocking positions before complaint was issued or else settlement of the cases by consent orders.

Nevertheless, in the 60 years since the enactment of Section 8 there have been numerous interlocks of the kind that the Section forbids, with only infrequent attack upon them by the enforcement agencies. The sporadic enforcement probably has been due chiefly in the fact that, as will appear below, the gaps in the law have been such that evasion has been easy, so that the law has seemed scarcely worth enforcing, and that some important types of restrictive interlock

are clearly beyond the law's intended reach. Recurrent surveys of all types of interlocks have shown that interlocks have proliferated, apparently becoming more numerous with passing time, so that the total problem they present as to intercorporate links is much larger than was envisaged in 1914 in section 8.[3]

Recently those who enforce the antitrust laws have undertaken or are contemplating experiments with legal theories, not yet adequately tested, that may restore the law's vitality and broaden the field to which it is applicable. The experiment that has been undertaken is enlargement of the interpretation of Section 8. That which is contemplated is to fill the legal gap by use of Section 5 of the Federal Trade Commission Act. This account of policy toward interlocks will end by summarizing the experimentation.

First, however, I must discuss the scope of the law as it has been traditionally interpreted, for only thus can one understand the prevalence of interlocks, the lethargy of the antitrust agencies in challenging those that are clearly prohibited, and the possible significance of the experiments.

As traditionally interpreted, the law of interlocking directorates lacks both adequate means and adequate scope to prevent such corporate links from being used to restrain trade among competitors. The following defects are obvious.

1. The prohibition applies narrowly to identical persons who hold the interlocking positions.

a) It does not apply to directors who, though different persons, have enduring and reliable personal ties to one another. Thus directorships in competing corporations are not

forbidden if they are held respectively by husband and wife, siblings, or parent and child.

b) It does not apply to directors who, though different persons, are closely associated by business interest and business activity. Thus directorships in competing corporations are not forbidden if they are held respectively by different partners in a business partnership, different executives of the same business corporation, a principal and his agent, a business executive and his employee, or a business executive and such a professional associate as his lawyer or his advertising manager.

2. The prohibition applies narrowly to links by directorships only.

a) It is not applicable if a single person controls two or more ostensibly competing corporations by stock ownership, but is not director of either; or controls two by stock ownership and is director of only one; or controls one by stock ownership only and is director of the other.

b) It is not applicable if a single person who is executive but not director of the one corporation is director of a competing corporation; or if that person is executive of more than one such corporation, but director of none.

3. The prohibition applies only to corporations that are or have been competitors. It has no application to preventative interlocks by which two or more corporations that are not competitors but could become so might be influenced to refrain from doing so.

4. The prohibition envisages corporations as discreet entities, not as possible parts of corporate combines, and hence leaves obscure the status of directorships that link parts of such combines. Nothing in it is explicitly or clearly applicable to interlocks by which the same person

is director of a corporation and also of a subsidiary, parent, or affiliate of another corporation that competes with this corporation. Neither is anything in the prohibition explicitly or clearly applicable to interlocks by which the same person is director of subsidiaries of competing corporate parents. Nothing in the prohibition gives guidance as to the legal significance of the degree of corporate stock ownership, or the degree of direction actually exercised over a subsidiary by a parent, in applying the prohibition upstream or downstream.

5. The prohibition also leaves obscure the extent of its application to the corporations that are linked by common directors. Its wording explicitly applies to the persons who are directors, not to the corporations that are thus linked. Corporations are not commanded to refrain from establishing the forbidden linkages. Indeed, if legal proceedings force particular directors to terminate their forbidden directorships, the corporations involved are not explicitly forbidden to re-establish the links through other directors. The prohibition can be enforced by courts by proceedings in equity, and thus benefits from the broad judicial power to make orders effective. It can also be enforced by the Federal Trade Commission, which is given statutory authority not only to require a violator to cease and desist from his violation but also to order "such person... to rid itself of the directors chosen contrary to the provisions" of Section 8.[4] Corrective orders, therefore, can be reasonably made broad enough to prevent corporations from re-establishing linkages that they can be required to terminate. Recent consent orders by this Commission have imposed upon the corporations involved requirements as to information that are based upon imputation of a corporate duty to avoid illegal interlocks. In 1973, for example, General Electric was ordered to require, for five years, that its directors and candidates for directorships

submit to the company a list of the principal products made by the other firms of which they are directors. It is noteworthy, however, that such requirements have been included in orders only in cases settled by consent.[5] Thus far only one injunction has been issued by a court. In it, rejecting the government's request for a broader injunction, the court limited its requirement to a) an order that the defendant director resign his directorship in one of the two corporations involved, and b) an order that the corporation from which he resigned accept his resignation and not permit him again to be a director.[6] It is doubtful that orders in such cases can be sufficiently comprehensive to block all of the gaps in the prohibition that have been mentioned above, even where violation has been proved and there is need to prevent future evasion.

Litigation as to obscurities has been insufficient to establish the law's meaning, presumably because the narrowness of the prohibition has made evasion so easy that clarification of what was obscure has not been worth the effort. Such decisions as there have been indicate that the prohibition applies where corporations are or have been competitors, unless the degree of their competition was trivial or there is no "present ability to resume" it, but that the prohibition does not apply where corporations are only potential competitors, nor where their relation to one another is not horizontal but vertical.[7]

Proceedings to enforce Section 8 have not been numerous, though they have been undertaken sporadically, and most of them have been settled informally by resignations or formally by consent orders, procedures that do not clarify obscurities.[8] Before 1972 the Federal Trade Commission issued 13 complaints under Section 8. In all but one of these cases, the interlock was termi-

nated by resignation and the complaint was then dismissed without order. In one instance where there was no resignation, an order was issued. Similarly, the Department of Justice, which issued five complaints, dismissed four of them after resignations.[9] The typical investigation has been one in which interlocking directors in competing companies, with their directorships under scrutiny, have abandoned all or all but one of these directorships without resistance. In 1952, apparently as a result of a report on interlocking directorates by the Federal Trade Commission,[10] the Department of Justice announced that it would try to get violators to comply voluntarily. In the early 1950's, it accepted several consent decrees that covered somewhat more than Section 8 explicitly forbids.[11] Search for voluntary consent appears to still be its policy. In 1968, it announced that of 16 interlocks that it had challenged, 11 had been terminated voluntarily.[12]

The reasons for official neglect of violations are illustrated by testimony of a former chairman of the Federal Trade Commission before a subcommittee of a committee of the House of Representatives:[13]

> ... several years ago the board of directors of General Steel Castings contained the president and two vice presidents of American Steel Foundries, all of whom were also directors of the latter company, and also contained the chairman of the board and the president of Baldwin Locomotive, both of whom were also directors of that company. When the Department of Justice questioned these interlocking directorates, the directors from American Steel Foundries and Baldwin withdrew from the General Steel Castings board. There is a catch. Their place was taken by two vice presidents of

Baldwin Locomotive, but since none of these officials was a director in any of these companies but General Steel Castings, the new arrangement satisfied the requirements of Section 8 of the Clayton Act. There is no reason to believe that the closeness of the executive and policy-making ties between the three companies was in any way reduced by the change.

The fact that interlocks to which Section 8 is applicable are only those that are direct interlocks has been in itself a serious obstacle to effective use of it against links between competitors, apart from the gaps and obscurities that have been discussed above. The prohibition does not bar competing corporations from being linked indirectly through the presence of different individuals from them (whether executives or directors) upon the boards of corporations with which neither of them competes. Such relationships are common. At least two types of them may restrain competition between competitors significantly.

First, competing corporations may have different directors upon the board of an enterprise that is vertically related to each of them as a significant supplier or customer. In that case, their joint presence on the board of that enterprise may become a means by which they negotiate allocations of supply or terms of transactions of purchase or sale that would be illegal if incorporated in contracts between the competing corporations. Secondly, different directors or executives of competing corporations may be on the board of a bank, or conversely, different officers of the bank may be on the boards of competing corporations. In such instances, the links may become means by which the bank's influence reduces the vigour of competition between the competing debtor corporations, or may have

effect upon the relative terms on which credit is available from the bank to these corporations and other borrowers. Thus by vertical links competing corporations may be horizontally linked by indirection, with restrictive results.

In addition to this gap in control over restrictive linkages among competing corporations, vertical ties between corporations may give rise, like vertical contracts and vertical mergers, to various antitrust problems, exclusive or preferential dealing, tying relationships, reciprocity, and leverage in making contracts. Section 8 makes no effort to cover such vertical problems.

Though recurrent investigations have shown that interlocking directorates have proliferated and through time have increased, appraisals of these relationships have rested upon common sense inferences. However persuasive these appraisals are, they do not rest upon hard facts derived from investigation of particular links. The staff of the Antitrust Subcommittee of the House Committee on the Judiciary reported in 1965 that "as of this time, there are virtually no factual analyses of how interlocking business organizations deal with particular transactions and the social and economic impact of such transactions."[14] Similarly, in 1973, the director of the Federal Trade Commission's Bureau of Competition said publicly, that: "Much of the discussion on interlocking directorates is intuitive and based on what is considered to be common sense observation or the self-evident conclusions of an analysis of the structure of organizations with management interlocks,"[15] and that "all of the conclusions about the potential effects of vertical interlocking arrangements share a common weakness; there is an absence of hard evidence on the actual impact to support them."[16]

The nature of these analytical common sense conclusions, as set forth in a study by the staff of the Federal Trade Commission in 1951, was summarized this year by him as follows:[17]

> (1) Interlocking directorates between competitors, whether on a direct or indirect basis, tend to limit or eliminate competition between the competing concerns. (2) Interlocking relationships between companies in the same or in closely related industries, but not in competition with each other, may forestall the development of competition which otherwise would come from normal expansion of the list of products which they manufacture. (3) Interlocking relations between companies that face similar problems, for example, the large integrated oil companies, or between companies in an industry and financial institutions that are broadly interested in that industry or in related industries, may give rise to communities of interest and create a united front against any who threaten habitual relationships or established preeminence. (4) Vertical interlocks may reach back to companies from which important supplies come and thereby evoke preferential treatment in the distribution of materials in short supply. (5) Vertical interlocks may reach forward to companies that consume or distribute the products of another and thus create preferential access to market outlets. (6) Interlocking relations between manufacturing corporations and financial institutions, especially banks and insurance companies, may establish a type of vertical relation that assures adequate credit to favored companies and a withholding of credit and capital from their competitors. (7) Interlocking relations may give expression to an underlying ownership interest and may involve nothing more than

a desire to protect an investment.

Where interlocking relationships have resulted in restraints of trade affecting interstate commerce, or have been means by which such restraints have been effectuated, action against them does not require use of Section 8. The Sherman Act forbids the restraints, and in a proceeding under the act the court can issue orders broad enough to provide an appropriate remedy. In appropriate Sherman Act cases, judicial orders have terminated and forbidden defendant enterprises to renew not only interlocking directorates but also links through employees and through stock ownership. The narrowness of Section 8 is significant only where the purpose of the proceedings is precautionary rather than remedial.

Experiments with Broader Action

Currently both the Federal Trade Commission and the Department of Justice are experimenting with ways of making the law as to interlocking directorates more effective.

The Department of Justice, which with the Federal Trade Commission shares jurisdiction to initiate proceedings under the Clayton Act, has brought an experimental proceeding under Section 8 which, for the first time, seeks to use the law against indirect interlocks. The Department contends that the different persons who hold directorships in two competing corporations are deputies of the corporation from which they come, and in support of this view relies upon Section 16 (b) of the Securities Exchange Act of 1954, under which a corporation may be deemed to act on the board of directors of another corporation through a deputy. It contends that the defendant corporation, through deputies, holds interlocking directorates. The challenged directorships are in two parent

companies, one of which allegedly competes with a wholly-owned subsidiary of another both directly and through one of its own wholly-owned subsidiaries. Thus the case poses two theories novel to Section 8 that a corporation, through deputies, may be a director, and that corporations may be regarded as competing through competition between their (wholly-owned) subsidiaries. In denying a motion for summary judgment, the court treated both issues as ones of fact, to be settled after trial. Proceedings are not yet concluded.[18]

If the Department wins affirmation of its contentions in this case, some of the limitations of Section 8 as described above may no longer exist. Corporations can be treated as directors through their personnel, presumably whether the persons involved are their directors or their other officials. The separate corporate identity of different parts of a corporate combine will not be relevant where a wholly-owned corporation is the creature of its parent, and possibly also in other instances in which one corporation is effectively controlled by another. These changes may make the law considerably more significant.

However, by themselves they will not remove all of the weaknesses of Section 8. They will not make the section applicable to links by different members of the same family; to links in which a directorship in one corporation is held by a person who personally owns stock in another; nor to links that involve different partners in a partnership. Neither will they make the law applicable to links among corporations that are potential but not actual or past competitors. They will not bring under the law links that create vertical restraints.

The Federal Trade Commission, which applies the Federal Trade Commission Act as well as the

Clayton Act, is contemplating, but has not yet actually undertaken, use of the latter in proceedings about interlocking directorates. Under the Federal Trade Commission Act, it has broad power to find that specified business conduct is an unfair method of competition. The Supreme Court has repeatedly held that this Act "was designed to supplement and bolster the Sherman Act and the Clayton Act...to stop in their incipiency acts and practices which, when full blown, would violate those Acts, as well as to condemn as 'unfair methods of competition' existing violations of them."[19] It has held that the Commission's broad power to declare trade practices unfair "is particularly well established with regard to trade practices which conflict with the basic policies of the Sherman and Clayton Acts even though such practices may not actually violate these laws."[20] Relying on these and other decisions, the present director of the Commission's Bureau of Competition recently said in a public speech that, in his opinion, "Section 5 of the FTC Act can reach and cure the majority of interlocking arrangements, irrespective of their legal status under Section 8, if they can be shown to injure competition or consumers, or if it can be shown that if they are not cured there is a strong possibility that they may lead to outright violation of the antitrust laws. With few exceptions, therefore, I think the Commission has the power to deal with specific instances in which vertical and indirect interlocks are found to be anticompetitive or found to serve as a vehicle for promotion of anticompetitive activities."[21]

With the prospect of such a legal tool, the Commission has begun to examine personal interlocks and related types of links between corporations, with focus upon three fields:

a) the food industries; b) the energy industries, and c) the relation between financial institutions and industrial decision-making, particularly as to mergers, joint ventures, and corporate take-overs. Its Bureau of Competition is considering formulation of a request to the Commission that it use its power under Section 6(b) of the Federal Trade Commission Act to facilitate work on such interlocks by requiring that corporations file annual reports of their interlocks and their ownership.[22]

If the Commission undertakes to use Section 5 against linkages between corporations, the scope of the effort and the probable degree of success in it are not yet clear. Obviously, however, two problems, legally distinguishable, are involved. As to relationships between competing corporations, the basic policies of Section 8 are clear, and the question is how far the Commission will choose to go and can go in applying them a) to types of personal interlock that are immune to that Section; b) to indirect links between competitors that lie beyond that Section's scope, and c) to potential as well as actual competition. As to vertical restraints, however, Section 8 contains no prohibitions and expresses no policy. For these the relevant question is how far the Commission will choose to go and can go in interpreting interlocks as inconsistent with policies of other parts of the antitrust laws, e.g., the condemnation of anticompetitive exclusive dealing and tying arrangements by Section 3 of the Clayton Act; the condemnation of anticompetitive vertical mergers by Section 7 of the Clayton Act; the condemnation of vertical restrictive agreements by Section 1 of the Sherman Act, and the condemnation of price discrimination and discrimination in related services and payments by the Robinson-Patman Act.

Moreover, to an unexplored extent the Commission may have power, even where it cannot regard a corporate interlock as an incipient violation of the Acts just mentioned nor as in conflict with the policies of those Acts, to terminate an interlock as an unfair method of competition forbidden by Section 5 of the Federal Trade Commission Act. If this power exists and should prove to be broadly useable, there is no obvious reason to assume that it would be applicable to personal interlocks only, as distinguished from other devices by which ties between corporations can be created and maintained. It might become a flexible form of attack upon the entire range of anti-competitive links. In using it, the Commission would benefit from the fact that its findings of fact are final if supported by evidence, so review of the decisions by the courts would be limited to interpretations of law.

VI - INTERLOCKING DIRECTORATES

Footnotes

1. Regulatory legislation, not only in the Clayton Act but also in other laws, has included provisions about interlocking directorates applicable to banks and other financial institutions; common carriers by rail, water, and air; communication enterprises; investment companies; security markets; power companies and suppliers of their equipment, and alcoholic liquor. These are summarized in James T. Halverson, "Interlocking Directorates - A Government View", remarks at Loyola College, Baltimore April 8, 1975 (duplicated), pp. 4-5.

2. The Act had only part of the scope that had been recommended in President Wilson's message to Congress, which requested that it prohibit interlocks among great corporations that had the effects of "making those who borrow and those who lend practically one and the same, those who sell and those who buy but the same persons trading with one another under different names and in different combinations, and those who affect to compete in fact partners and masters of some whole field of business." See House Report 627, 63rd Congress, 2nd Session, May 16, 1914.

3. Official studies of interlocking directorates include the following: Disclosure of Ownership, Senate Document 93-62, 93rd Congress Second Session, March 1974; Interlocks in Corporate Management, staff report, Antitrust Sub-committee, House Committee on the Judiciary, 1965; Report on Interlocking Directorates, Federal Trade Commission, 1951.

4. Section 11 of the Clayton Act.

5. The order gainst General Electric appears in Docket C-2477. Similar though not identical orders have been issued against Chrysler (Docket C-2484), and against the Aluminum Company of America, Armco, and Kennecott (Dockets C-2415, C-2416, C-2417, and C-2418).

6. U.S. v. Sears Roebuck and Co., 111 F. Supp. 614 (S.D. N.Y., 1953).

7. Ibid., also U.S. v. Grant Co., 345 U.S. 629 (1953) and Paramount Pictures Corp. v. Baldwin-Montrose Chemical Co., 1966 Trade Cases #71,678 (S.D.N.Y., 1966).

8. In 1947, the Department of Justice announced that in a survey of interlocking directorates it had found about 1,500 persons holding directorships in more than one firm, and that most of them whose directorships were illegally interlocked resigned without contest. See Victor Kramer, "Interlocking Directorships and the Clayton Act after 35 Years", 59 Yale L.J., 1266, 1270-71 (1950).

9. The Commission's consent order against Union Bag and Paper Corp., appears in 52 FTC 1278 (1956). The case by the Department of Justice that was not dismissed is cited in note 6 above.

10. See note 3 above.

11. U.S. v. General Outdoor Advertising Co., 1955 Trade Cases #68,169; U.S. v. Liberty National Life Insurance Co., 1954 Trade Cases #67,801; U.S. v. Liquid Carbonic Corp., 1952-1953 Trade Cases

#67,248.

12. Press release, February 27, 1952. Press release, June 27, 1968.

13. Testimony by James M. Mead before Subcommittee on Study of Monopoly Power, House Committee on the Judiciary, 83rd Congress, 1st Session, quoted by Halverson, _op. cit._, pp. 11-12.

14. _Interlocks in Corporate Management_, _op. cit._, note 3.

15. Halverson, _op. cit._, note 1, p.2.

16. _Ibid_, p. 17.

17. _Ibid_, p. 22, summarizing page 23 of the 1951 report mentioned in note 3 above.

18. U.S. v. Cleveland Trust Co., 1974 -- 2 Trade Cases. #75,278 (N.D. Ohio, 1974). Since this case pertains to interlocking banks, it is subject to legislation that differs in various respects from that generally applicable to corporations. As to the point under discussion, the differences do not seem to be relevant. However, the complaint alleges that the companies involved are also linked by substantial amounts of stockholding by Cleveland Trust, so that the attack upon them under Section 8 has a special setting of other alleged ties.

19. F.T.C. v. Motion Picture Advertising Service Co, Inc., 344 U.S. 392 (1953). This passage was quoted with approval by the Court in the case mentioned in the next footnote.

20. F.T.C. v. Brown Shoe Co., 384 U.S. 316 (1966), at 321.

21. Halverson, op. cit., note 1, pp. 20-21.

22. Ibid, pp. 26-30.

V11 - MERGERS

The ensuing discussion pertains to policy about union of the assets of two or more enterprises by merger or acquisition. For convenience, the discussion will call such unions mergers, using this term as a generic one that includes all such unions, both those that are mergers in the sense that at least one enterprise ceases to exist, and those that are acquisitions in the sense that the enterprises involved continue to exist. Where the form of the union is relevant, it will be identified by descriptive terms such as acquisition of stock, acquisition of assets, and joint ventures; but the term merger, when not qualified, should be understood to include all of these.

Mergers, important in particular industries from 1890 to 1900, spread over large parts of American industry in the period 1919-1930. By mergers, during this period, more than 8,000 enterprises in manufacturing and mining ceased to exist; more than 10,000 retail stores were absorbed into chains, and nearly 2,800 public utility enterprises and nearly 1,100 banks disappeared.[1] Mergers became a major aspect of industrial structure.

Existing Legislation to Control Mergers

Special legislation designed to control mergers, first enacted in 1914 before the proliferation of mergers in the 1920's, was greatly strengthened in 1950 in an effort to remove the defects of the 1914 law. Action under the 1950 version is now a major part of the work of both of the Federal antitrust agencies. Almost 30 per cent of all antitrust cases instituted by the Department of Justice in the years 1963-1970 consisted of or included

a challenge to one or more mergers, and mergers have become similarly important in proceedings by the Federal Trade Commission. In both versions of Section 7 of the Clayton Act it is applicable to partial acquisitions of stock or assets, but this fact has little practical importance.[2]

Before 1914, mergers were subject to the Sherman Act only. Like all other business combinations, they could be dissolved or subjected to corrective orders under Section 1 if they resulted in restraint of interstate commerce, and under Section 2 if they were attempts to monopolize some part of interstate commerce or achieved such a monopoly. Proceedings under this Act between 1904 and 1922 twice prevented a great railroad to the Pacific Coast from acquiring control of a great competitor by stock purchases, and twice prevented holding companies from controlling major competing subsidiaries - railroads in both instances and also coal companies in one of them.[3]

In appropriate instances the Sherman Act continues to be used. But in using it, success is possible only under two conditions: either that a merger has already resulted in substantial and provable restraint or that, though there is not yet proof of such restraint, the merger was of such a magnitude and appeared in such a setting that the court will regard substantial restraint as inevitable or monopolization as attempted. Instances of the second kind are few, and a case so oriented has formidable problems. In one case lost by the government, the court said that the dollar volume of the business involved is not compelling, but that relevant matters include "the percentage of business controlled, the strength of the remaining competition, whether the action springs from business requirements or purpose to monopolize, the probable development of the industry,

consumer demands, and other characteristics of the market... The relative effect of percentage command of a market varies with the setting in which that factor is placed."[4] To get adequate proof as to such matters would be difficult, expensive, and slow, and hence proceedings would be necessarily few.

The 1914 version of Section 7 of the Clayton Act was intended to facilitate control of mergers. It required proof of probable effect instead of proof of existing or inevitable effect;[5] expanded the relevant concept of effect to include not only restraint of commerce but also substantial lessening of competition and tendency to create a monopoly, and sought to cover not only effects upon the market but also effects limited to relationships between the corporations involved in the acquisition.[6] However, it was applicable only to stock acquisitions, which until that time had been the only significant types of acquisitions.

This version of Section 7 failed almost completely to accomplish its purpose. Acquisitions became typically acquisitions of assets instead of acquisitions of stock. Where stock acquisitions were used as means to get the power to make acquisitions of assets, the courts held that, if the asset acquisition was accomplished before an order was made against the stock acquisition, the asset acquisition was immune even though accomplished by forbidden means.[7] The Supreme Court deprived of significance the test of effect on competition between the corporations involved: by holding that if competition between these corporations was not substantial in the market sense this competition could not be substantially reduced, it substituted a test of effect in the market -- in effect, the Sherman Act test -- for the narrower test

that the language of the law had seemed to apply.[8]

Application of the 1914 law was limited further by assumption, found later to be erroneous, that the law did not cover vertical mergers.[9] Such mergers became numerous.

For a decade and a half, beginning in the 1930's, the Federal Trade Commission recommended that Section 7 be revised; but the depression of the 1930's and the second World War absorbed Congressional attention, and action was delayed until 1950.[10] In that year, Section 7 was substantially amended. Except in cases in which the Federal Trade Commission Act is used to supplement this Section (which will be discussed below), the amended version is now the chief instrument of merger policy both in the Federal Trade Commission and in the Department of Justice.

Strengthening of Legislation in 1950. The three important changes of the 1950 version were: first, for all corporations subject to the jurisdiction of the Federal Trade Commission (but not for other corporations),[11] the law was made applicable to acquisitions of assets as well as of stock. Secondly, the language about competition between the acquiring and the acquired was deleted. This change was explained, not as mere elimination of words that judicial decisions had deprived of meaning, but as a way of removing doubt that small corporations could make harmless mergers. The committee reports emphasized, however, intention that the statute be used not merely against effects of Sherman-Act magnitude but wherever there was incipiency of anticompetitive effects. Thirdly, the test of legality was modified. It now forbids

acquisitions "where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly." Committee reports emphasized the intention that the law would be applicable to vertical and conglomerate mergers as well as horizontal ones.[12]

Underlying the amended version were two purposes. The first, fully developed and clearly expressed, was to use merger law more effectively by stopping in their incipiency, structural changes in particular markets that were anticompetitive in tendency. The second purpose, evident in public reports by the Federal Trade Commission and others and in the statement that the amendment applied to conglomerate mergers, was still developing. Its relation to the amended law was not explicit in that law's text nor clearly formulated as a consensus by the Congress that enacted it. This was a purpose to retard and if possible reverse what was believed to be a broad trend toward concentration in the economy. Success in achieving the law's first purpose was indispensible but not necessarily adequate to achievement of the second. Whether or not consistent use of the law against anticompetitive tendencies in particular markets attributable to mergers in those markets would be enough to change the concentrative trend was uncertain; uncertain also was the degree to which consistent action would be possible with the resources that would be provided for application of the law.

The two purposes have been expressed in different programs of action focussed upon different kinds of mergers. The first purpose has resulted in proceedings by both the Department of Justice and the Federal Trade Commission against horizontal mergers, vertical

mergers, and mergers with potential competitors. The second, evident chiefly in the Federal Trade Commission except during a brief period, has resulted in proceedings against mergers that extended territorial markets or product markets or united firms in unrelated fields.

Since the character of the law becomes clearest in proceedings of the first kind, these will be discussed first. First, it was applicable only to acquisitions in which both of the enterprises involved were corporations. A large corporation could acquire individual proprietorships and partnerships without concern about Section 7. Secondly, it was limited to instances in which the acquiring corporation, the corporation from which the acquisition was made, and the effect of the acquisition were each in interstate commerce. Thus a large corporation could disregard it in acquiring enterprises so localized as to be only intra-state. Because of these limits it was defective as a legal instrument to curb grocery chains if they expanded by acquiring numerous grocery stores, or to block absorption of local dairies by large manufacturers of dairy products.

Since neither of these limitations exists in the Federal Trade Commission Act, the Commission has avoided them, where it objects to mergers that are not reachable under the Clayton Act, by proceeding under Section 5 of its own statute. This section forbids unfair methods of competition and unfair acts and practices, and one of its purposes, the courts have held, is to stop activities contrary to the purpose and spirit of the antitrust laws.[13] In a proceeding against numerous acquisitions by a large dairy company, violation of both Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act will be alleged. The former section will be used against acquisitions of other corporations that do interstate business;

the latter Section against acquisitions of partnerships, individual proprietorships, and small local enterprises.

Shortly after Section 7 was amended, a decision by the Supreme Court changed substantially the significance through time that had been thought to be applicable to stock acquisitions under the old version of the law, and did so in a respect presumably applicable to the new version also. The Court had before it a charge under Section 7 based upon the acquisition of 23 per cent of the stock of General Motors in 1920 and earlier. After the acquisition, General Motors had acquired its outstanding position in the automobile industry, and DuPont's relation to it as supplier had been one of the sources of DuPont's growth in the chemical industries. In deciding that the acquisition violated Section 7, the Court held that incipiency, as relevant to Section 7, "denotes not the time the stock was acquired but any time when the acquisition threatens to ripen into a prohibited effect...Prior cases under Section 7 were brought at or near the time of acquisition... None of these cases holds, or even suggests, that the Government is foreclosed from bringing the action at any time when a threat of the prohibited effects is evident... We repeat, that the test of a violation of Section 7 is whether at the time of suit there is a reasonable probability that the acquisition is likely to result in the condemned restraints."[14]

By virtue of this decision, an enterprise that now acquires a substantial part of the stock of a supplier or purchaser presumably faces not only whatever legal vulnerability may exist at the time of the acquisition, but also has (like the holder of a substantial amount of stock in a similar company acquired

since 1914) a contingent risk if subsequent developments increase the significance of the acquired stock.

As amended, Section 7 leaves undefined the meaning of the term "section of the country." The accompanying committee reports made clear that this term was intended to apply to any area, however small, if it was a significant and coherent unit economically and was large enough for operation in it to be part of interstate commerce. Those who enforce the law have assumed that the term is equivalent to the concept of a relevant territorial market. The Department of Justice has defined it as follows:

"The total sales of a product or service in any commercially significant section of the country (even as small as a single community), or aggregate of such sections, will ordinarily constitute a geographic market if firms engaged in selling the product make significant sales of the product to purchasers in the section or sections. The market need not be enlarged beyond any section meeting the foregoing test unless it clearly appears that there is no economic barrier (e.g., significant transportation costs, lack of distribution facilities, customer inconvenience, or established consumer preference for existing products) that hinders the sale from outside the section to purchasers within the section; nor need the market be contracted to exclude some portion of the product sales made inside any section meeting the foregoing test unless it clearly appears that the portion of sales in question is made to a group of purchasers separated by a substantial economic barrier from the purchasers to whom the rest of the sales are made."[15]

Similarly, those who apply the law have assumed that the statutory phrase "line of

commerce" is equivalent to the concept of a product or service or a coherent group of products or services. In the words of the Department of Justice: "The sales of any product or service which is distinguishable as a matter of commercial practice from other products or services will ordinarily constitute a relevant product market, even though, from the standpoint of most purchasers, other products may be reasonably, but not perfectly, interchangeable with it in terms of price, quality, and use. On the other hand, the sales of two distinct products to a particular group of purchasers can also appropriately be grouped into a single market where the two products are reasonably interchangeable for that group in terms of price, quality and use. In this latter case, however, it may be necessary also to include in that market the sales of one or more other products which are equally interchangeable with the two products in terms of price, quality, and use from the standpoint of that group of purchasers for whom the two products are interchangeable."[16]

An initial step in applying the law is to define the relevant market in its territorial and commodity aspects. Within this market one must look for the effects that, if found, make the acquisition illegal. The definition of the market may be crucial to a merger proceeding. The larger the market, the smaller will be the percentage of it that is united by the acquisition and the smaller the possibility that this union will have substantial effects. The smaller the market, the greater will be the possibility that what was acquired lies outside that market and has no direct effect upon competition within it. When a merger is challenged, the challenging authority has defined the market to its own satisfaction and thinks that it has found anticompetitive proba-

bilities there. Resistance to the challenge typically includes claims that the market is actually much larger or much smaller than has been alleged, and that the evidence as to probable effect depends for its persuasiveness upon distortion of the market definition. Thus disputes over market definition have become common in controverted merger cases. Decisions determine such questions as whether automotive fabrics and finishes are sufficiently different from other fabrics and finishes to be a line of commerce;[17] whether children's shoes as a group are a line of commerce or must be divided into lines that differ for children of different sexes and ages;[18] and whether glass containers and cans can be treated as a single line of commerce.[19] Similarly there are decisions whether the relevant territorial market is national, regional, or local,[20] and what are the boundaries of an urban market area.[21]

In such decisions, efforts are made to define markets so that the definition corresponds to commercial realities and is economically significant. There is no precise standard for such decisions. Several considerations are deemed pertinent. In the guiding case, which pertained to a merger in the shoe industry, the Supreme Court accepted the idea that a broad market can be relevant yet divided into submarkets that are also relevant: "The outer boundaries of the product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. However, within this broad market, well-defined sub-markets may exist which, in themselves, constitute product markets for antitrust purposes... The boundaries of such a sub-market may be determined by examining such practical indicia as industry or public recognition of the sub-market as a separate economic entity, the product's peculiar characteristics and uses, unique production faci-

lities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors."[22]

Though in defining markets, emphasis usually has been placed upon relationships from the point of view of buyers, such as interchangeability of products in use and consequent cross-elasticity of demand, decisions have not ignored relationships among suppliers. Uniqueness of production facilities and specialization of vendors are both mentioned in the passage quoted above. Peculiarities in the manufacturing process were considered relevant to the decision about automobile fabrics and finishes mentioned above. When the firms involved in an acquisition operate in only part of the territory or only part of the product field that is usually thought to be the relevant market, the field in which their operations overlap, if large enough to be significant, is considered the market relevant to the particular case.[23]

The cases show clearly that the courts are aware of the need to keep market analysis simple enough to make adjudication possible within reasonable limits of time and effort. In the Philadelphia Bank case, for example, it was obvious that different kinds of financial service were offered by groups of competitors that were not identical and that in the field of commercial banking the larger lending transactions involved competition over wider territorial areas than the smaller ones.[24] The court simplified its decision by treating commercial banking as the relevant field, and by deciding, after considering the wide area appropriate to large customers and the small areas appropriate to small ones, that a "workable compromise" was to regard the area as the four metropolitan counties of Philadelphia.

If an acquisition is likely to diminish competition any where, the acquisition is forbidden. The guiding principle, therefore, is to consider appropriate whatever concept of the market discloses and identifies a significant anticompetitive impact from the acquisition.[25] In words of the Department of Justice, "In enforcing Section 7 the Department seeks primarily to prevent mergers which change market structure in a direction likely to create a power to behave non-competitively in the production and sale of any particular product, even though that power will ultimately be limited, though not nullified, by the presence of other similar products that, while reasonably interchangeable, are less than perfect substitutes. It is in no way inconsistent with this effort also to pursue a policy designed to prohibit mergers between firms selling distinct products where the result of the merger may be to create or enhance the companies' market power due to the fact that the products, though not perfectly substitutable by purchasers, are significant enough alternatives to constitute substantial competitive influences on the production, development or sale of each."[26]

Problems in Enforcing Legislation

As enforcement of the revised version of Section 7 began, several problems became acute. The first of these was the need to obtain certain types of information that were necessary in merger cases. It was clear that one matter relevant to the probable effect of a merger was the share of the market that the acquirer possessed after the merger. To ascertain this share, the size of the market must be measured both as to relevant products and as to relevant territory. Voluminous information was available from official sources about the locations of productive facilities and the amounts produced there.

But this information was usually defective for measurement of markets: a) though compiled in such a way that it would provide data about product groups of different degrees of inclusiveness and about territories both large and small, the boundaries of the statistical categories for which information was available were unlikely to provide data that neatly fitted the boundaries of a market relevant to a particular merger case; b) government rules intended to assure privacy of business information require that some important kinds of data about productive activity be not made available except in compilations for at least four producers; and when there was need for totals for small areas such as counties, or for broader areas that contained few producers, the limits upon disclosure might make that information unavailable because the firms there were fewer than four; c) even more serious was the difficulty that most official information pertained to places where goods were produced, whereas those who were concerned about market shares wanted to know where the goods were sold. Production statistics did not show how much of what an area produced was sent to other areas for sale, nor how much produced elsewhere was imported into the relevant area. Hence such figures could not be used where sales that penetrated the productive areas of other producers were substantial.

Because of such limitations in official statistics, many enterprises involved in mergers had for some time before the merger used privately prepared statistics or estimates about the size of markets relevant to their activities. Sometimes these were their own compilations and estimates; sometimes those of a trade association, a management advisory service, or some other commercial undertaken. If the defendants in a merger case had been using the information for their own business purposes, it presumptively

was the best information available, and thus was arguably appropriate for use in the merger proceeding. Nevertheless, such information obviously differed from case to case in quality and adequacy, and was open to doubt about its reliability and bias. This kind of question came to focus in the Pillsbury case, one of the early cases considered by the Federal Trade Commission, when, no appropriate official statistics being available, the attorney for the Commission tried to prove the size of the total market for the relevant products in the southeastern part of the United States by using data that had been used by the respondant but had been privately compiled. Rejecting the information as unreliable, the hearing examiner asked that the Commission use its power under Section 6(b) of the Federal Trade Commission Act to obtain from every producer of the products a statement of his sales of them in the area, compile the figures in these statements, and thus prove the size of the market in a reliable way. When the Commission's attorney refused to initiate such a procedure, the hearing examiner dismissed the case. When the dismissal was appealed to the Commission, it was over-ruled. But the Commission decided that it would not complicate its merger cases by assuming the burden of such _ad hoc_ statistical inquiries and of the legal challenges that recipients of such inquiries probably would institute against an attempt to use the Commission's authority in this way to require reports.[27]

The second problem was to make relevant statistical information, official or unofficial, acceptable under the rules of evidence. Problems similar in kind had arisen occasionally in other antitrust cases, but only in an occasional case about monopolization on less than a national scale had they involved need for

measures of a market upon which decision might turn. There were no generally accepted rules about the admissibility of such statistics. It was obvious that where official statistics seemed to be relevant to a case the deciding authority could not merely assume that all government figures were accurate and that in compiling them the relevant decisions about how to do this had been such that the results would be appropriate for the proceeding to be decided. It was far from obvious, however, what kind of evidence, presented by whom, would be adequate to accredit official figures.[28] It was even more obvious that tests as to quality and adequacy were appropriate in use of privately compiled data. It was necessary to explore case by case the way in which the particular data that seemed to be relevant could best be authenticated under the tests of accuracy and adequacy that are the essence of the rules of evidence. Decisions about admission of evidence and conditions requisite thereto were made, instance by instance, by judges and hearing examiners during proceedings.

The third problem which continues to be important, was the scope of the inquiry appropriate to merger cases. In such a case the question is what will be the probable future effect of a present change in the structure of business ownership. Since that probability is the result of many variables, a good answer seems to need wide exploration of the present facts and existing trends as to each of these variables. But so wide an inquiry would convert nearly every merger case into a big one, requiring large amounts of time and money to develop and present the evidence and also complex evaluations of the meaning and relative importance of diverse matters. Though such careful examination probably would result in a better decision in a particular case, it necessarily would

reduce the number of cases that could be considered and decided. It is true, of course, that similar complexity appears in decision of some other types of anti-trust cases, e.g., some of the cases involving monopolization; but whereas in other anti-trust fields such problems arise seldom, mergers are numerous and decisions about many of them involve predictions that might benefit from fuller exploration. Hence, both the deciding authorities and the prosecutors have found in the merger field peculiarly large incentives to develop acceptable "rules of thumb", that is, shortcuts to decision that would limit the cases to consideration of only a few important variables, about which the facts could be ascertained with only a moderate difficulty or could be determined by approximation or by sampling without serious distortion.[29] The content of some rules of thumb that have been accepted will appear below in accounts of certain merger decisions and of official policy statements.

The problems that have been summarized above gave rise to a fourth problem, that of the effect of delay in deciding a merger case upon the private and public interests involved. Delay in decision about a challenged merger affects the interests of the merged company (and of enterprises that deal or compete with it) because prior to decision of the case the interests of these firms are affected by uncertainty whether or not coordination of the previously separate activities of the merged firm will be terminated as unlawful; the longer the delay the more troublesome is the uncertainty to the private interests affected thereby. The public interest in restoring competition is also affected, for the longer the merged assets remain together, the greater the difficulty of restoring, in viable condition, the firm that temporarily did not exist. For such reasons,

both the government and the defendant typically share an interest in expediting decisions and in disposing of issues about mergers, so far as possible, before a legal proceeding is begun.

This incentive has led the antitrust agencies to explore the possibility of disposing of merger problems informally, and of developing more clearly formulated priorities. Both the Department of Justice and the Federal Trade Commission give advisory opinions, so worded as to deprive these of legal status, to enterprises that ask for them when contemplating mergers. The Commission, which can not only issue corrective orders, but also has, under Section 6 of its basic statute, general authority to require corporations to file reports, has repeatedly issued a requirement that prior reports of intended mergers be filed by corporations in a particular segment of the economy, and in 1969 made this requirement general for all large mergers by corporations under its jurisdiction.[30]

Both agencies also act in a way unusual in the antitrust field by making public official statements of their policy in enforcing the merger law. The Department's statement, obviously developed after careful consideration of its relation to relevant economic theories about industrial organization, covers the entire merger field, with separate parts about the chief types of mergers.[31] The Federal Trade Commission has issued five official statements thus far, each focussed upon a particular field of business in which it considered that mergers were numerous and important, and as to which it thought that it had acquired adequate expertise. The content of these policy statements will be discussed below where appropriate.

The incentive to prevent delay from reducing the chance to restore competition also has led both agencies to seek ways of keeping acquired companies viable during the pendency of a case in which a merger is challenged. In cases that it considers appropriate, the Department of Justice asks the courts for temporary injunctions designed to prevent acts by the acquirer that might cripple the acquired one if the latter were made once more independent, such acts as destroying, or otherwise reducing, the usefulness of the acquired productive facilities; ceasing to use, or changing the meaning of, acquired trademarks; or terminating direct distribution from acquired productive facilities to distributive enterprises that had been customers of the acquired firm. The Federal Trade Commission's procedures and its relation to the courts, initially ill-suited to such temporary injunctions, have been modified by law so that the Commission can also ask for temporary orders in appropriate cases.[32]

Impact of a Merger Upon Competition

The decisive question in a merger proceeding is the probable impact of the merger upon competition. This question requires that the decider estimate the future effect of a present change in the structure of control over an industry, a task difficult at best, and often made more difficult by technological and economic changes that, though obviously relevant and possibly clear in their present direction, are uncertain in speed, scope and duration. Such estimates have been made necessarily in the cases decided; and tentative generalizations have been derived from the decisions as guides for further decision-guides both for enterprises that are considering acquisitions and for the agencies that apply the law and strive for consistency in doing so. What follows will attempt to summarize these generalizations; but

the tentative nature of them must be emphasized.

Horizontal Mergers. The type of merger that involves the simplest decision is one in which the firms merged have competed with each other in the same market. If the acquisition merges their operations completely, one competitor is entirely eliminated. If capital assets are transferred from one to the other, the acquisition changes the relative importance of the operations of the two. If one acquires stock in the other, it attains some degree of influence upon the other's decisions. Regardless of the kind of acquisition, some direct effect upon competition is probable and usually is intended. Since the law forbids any substantial anticompetitive effect, the decision about the acquisition need not weigh claimed advantages against anticompetitive effects; it need only determine whether or not a substantial anticompetitive effect is probable. In such cases, the courts have been willing to infer anticompetitive effects where the firms involved had substantial market shares and the merger enhanced the share of the merged firm substantially. The appraisal appears clearly in the decision in the Philadelphia Bank case, in which the Supreme Court said: "Specifically, we think that a merger which produces a firm controlling an undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence showing that the merger is not likely to have such anticompetitive effects."[33] In this instance the percentage share was 30 per cent, and the increase in concentration 33 per cent.

When a large firm acquires a very small one, the problem is less easily decided. If the acquired enterprise has been a vigorous

competitor, initiating price reductions, or otherwise being a source of innovations, the acquisition probably will be condemned. If the acquisition has no such special significance, challenge to it becomes more likely the larger the acquiring firm, and this likelihood increases with increase in the size of the acquired firm. Previous involvement in antitrust proceedings tends, in practice, to weight the scales against the acquirer. So does a record of numerous acquisitions. Where there have been such acquisitions, the Federal Trade Commission is apt to include in its decision an order that for a stated period of time (usually from five to 10 years) the acquirer shall not make further acquisitions without prior approval.[34]

In a market in which the leading firms merge or in which merger creates a leading firm, anticompetitive probabilities may be seen in relatively small percentages of the market. Thus in Los Angeles, where the number of retail food stores had been declining and a trend toward concentration was evident, the courts condemned a merger of two chain groceries that had created the second largest chain in the area, with 7.5 per cent of the market.[35]

At such levels, the relative size of the merging enterprises, the number of competitors, the ease of entry into the market by others, and the trend of concentration have weight in the decision. If entry is easy and often takes place, mergers are likely to be thought less significant. Where entry is difficult, disparities in the size and strength of rival firms are considered obstacles to competition, so that reduction of such disparities by merger of small firms is regarded as pro-competitive. Mergers that diminish the number of firms are considered anticompetitive to a degree that grows as the remaining rivals become fewer.

Thus when small firms merge in a market that includes large firms, the merger usually has both pro-competitive and anticompetitive aspects. The goals of policy are clear: to prevent a competitive market from becoming an oligopolistic one and to foster vigorous independence among the competitors. Pursuit of these goals, however, involves trade-offs of opposing considerations. Unless the trend toward concentration is clear and is approaching dangerous levels of concentration, a merger will not be challenged if it is a union of small firms that diminishes the disparity between their size and that of their larger rivals and thereby enables them to compete more effectively.

Considerations like those described above were summarized as to horizontal mergers in guidelines published by the Department of Justice in May 1968.[36] These had several purposes: to give guidance to enterprises that contemplated mergers and to their lawyers; to formulate official policy in a way that would enhance consistency, and to provide a rationale that would enhance public support for the policy. These guidelines are currently in use.

As to horizontal mergers, the purposes are thus stated: "1) preventing elimination as an independent business entity of any company likely to have been a substantial competitive influence in a market; 11) preventing any company or small group of companies from obtaining a position of dominance in a market; 111) preventing significant increases in concentration in a market; and 1V) preserving significant possibilities for eventual deconcentration in a concentrated market."

Percentages of the market are said to have "primary significance" in pursuing these purposes. The larger the share of the acquired firm, "the more likely that it has been a substantial competitive influence" and that concentration in the market will be "significantly increased." The larger the market share of the acquiring firm, the more likely "that an acquisition will move it toward, or further entrench it in, a position of dominance or of shared market power." These probabilities are translated by the guidelines into percentages of the market held prior to the merger by the firms involved in the acquisition, with the statement that the Department "will ordinarily challenge" mergers that attain stated percentages. The percentages are so arranged that as the market share of the acquiring firm becomes larger the minimum size of the acquisition that will be challenged becomes smaller. That the environment affects the probabilities is recognized by applying different percentages to markets in which different degrees of concentration already exist.

For highly concentrated markets (defined as those in which the aggregate market share of the four leading firms is 75 per cent or more) three sets of percentages are given, with the statement that percentages not shown should be "interpolated proportionally" to those shown. Those given are as follows:

Acquiring Firm	Acquired Firm
4%	4% or more
10%	2% or more
15% or more	1% or more

Thus the Department expects to challenge even small acquisitions by a firm that already has 15 per cent of the market, if the acquisition results in a firm with at least 16 per cent, and excepts to challenge acquisitions that result in a firm as small as eight per cent of

the market if they involve an acquisition large enough to double the size of the acquiring firm. By treating as relevant both the size of the acquiring firm and the size of the acquisition, the guidelines have anomalous results as to the size of the firms that can be the result of a merger without challenge: if the acquirer is small, post-merger challenge begins at eight per cent; if the acquirer is large, the challenge begins at 16 per cent, a post-merger size twice as large.

For markets that, though concentrated, have aggregate percentages of less than 75 per cent for their four leading firms, the announced percentages are different. In these markets the percentages at which challenge ordinarily will begin are listed as follows:

Acquiring Firm	Acquired Firm
5%	5% or more
10%	4% or more
15%	3% or more
20%	2% or more
25% or more	1% or more

In these less concentrated industries, as compared with the more concentrated ones, larger acquisitions will remain unchallenged, and mergers may result in larger percentages before challenge begins. This listing, however, like the previous one, involves challenges of smaller percentages of acquisition as the acquiring firm becomes larger, and accepts without challenge larger firms after the merger when the acquiring firm is large than when it is small.

For industries still less concentrated, the standard changes. A trend toward concentration provides the guide, rather than the existing level of concentration. A trend toward concentration is said to be present where, in a period of from five to 10 years before the merger ("excluding any year in

which some abnormal fluctuation in market shares occured"), the aggregate market share of any group of from two to eight of the largest firms has increased by seven per cent or more. Where such a trend exists, the Department will challenge any acquisition by any member of this group in which the market share of the acquired firm is two per cent or more. Since the stated policy applies to all members of the concentrated group, it treats equally the largest and the smallest of them, and apparently applies even to a member of the group with an individual market share that has not increased or even has fallen during the period.

This part of the guidelines tries to make specific an intention to deter growth in concentration at an early stage by challenging horizontal mergers even when neither the acquiring firm nor the acquisition is large. Concentration having grown to the specified extent, any acquisition by a leading firm is to be subject to challenge if it enhances the concentration by as much as two per cent, even though, prior to that acquisition, the acquiring firm had not grown by merger or had not grown at all. Since the policy applies regardless of the level of the concentration that has recently increased by the specified amount, it could be applicable even where, at the time of the challenged merger, eight leading firms had an aggregate of no more than 18 or 20 per cent of the market and were not separated by a substantial gap in size from their smaller competitors. However, so far as I have been able to discover, the Department has not applied this part of its policy with that much severity.

In addition to emphasizing percentages as has been indicated above, the guidelines provide for attention to horizontal mergers that are deemed to have special significance on some other ground. The two types that are mentioned as most common are stated to be: a) acquisition

of a competitor that is "a particularly 'disturbing', 'disruptive', or otherwise unusually competitive" factor in the market, and b) "a merger involving a substantial firm and a firm which, despite an insubstantial market share, possesses an unusual competitive potential or has an asset that confers an unusual competitive advantage (for example, the acquisition by a leading firm of a newcomer having a patent on a significantly improved product or production process)."

The guidelines include a paragraph that rejects the claim that challenged mergers will produce economies, on the triple ground, a) that the standard for challenge " will usually result" in no challenge as to companies "operating significantly below the size necessary to achieve economies of scale"; b) that where substantial economies are possible they can normally be attained by internal expansion, and c) that proof of economies and their size involves "severe difficulties." Nevertheless, the rejection is not absolute, but applies "unless there are exceptional circumstances."

The statement of policy notes as an exception that mergers by a failing company will "ordinarily" not be challenged if there is "clear probability of a business failure" (as distinguished from loss of profit or position from difficulties that could be overcome by self-help), and if effort in good faith has not obtained a reasonable offer more consistent with the purposes of Section 7 by an acquirer that intends to keep the failing firm in the market. Where what is failing is a division of a multi-market company, the statement says the Department will apply the failing-company standard "only in the clearest of circumstances."

Vertical Mergers. Vertical mergers take two forms. In one, a so-called backward acquisition, an enterprise acquires one that sells what the

acquirer buys. Acquisition of a flour mill by a baking company would be a backward merger. In the other, a so-called forward acquisition, an enterprise acquires one that buys what the acquirer sells. Acquisition of a baking company by a flour mill would be a forward merger. As these examples suggest, backward and forward acquisitions may result in similar kinds of vertical integration.

Before a vertical merger, rival suppliers can compete for the user's purchases, and rival users can compete for the supplier's products. After the merger establishes a preferential relationship between the merging firms, products will typically flow from the merged supplier to the merged user to whatever extent self-supply is practicable, and the opportunities of other suppliers and users to deal with the merged firm will be reduced. If entry into the affected markets is easy, any unbalance that is created by the merger is likely to be merely transitional. But if entry is difficult, the unbalance may affect competition. In the language of the merger cases, the merger "forecloses" access by other users to the merged supply so far as the merged user needs that supply, and forecloses access by the other suppliers to the merged user so far as the merged supplier can provide what that user needs. If the foreclosure is trivial, no problem arises for competition policy. If it is substantial, there may be a problem. Such a problem is likely to appear when, either at the level of the supplier or at the level of the user, the foreclosure covers a large part of the total market. It is also likely to appear where shortage of supply or of demand makes interruption of the flow of goods peculiarly difficult for other non-integrated enterprises. In such instances, one vertical merger is likely to result in other precautionary vertical mergers by firms that fear the results of shortages that they foresee.

In the Brown shoe case, the first in which a Supreme Court opinion pertained to a merger under the revised version of Section 7, the relevant part of the Court's decision pertained to foreclosure.[37] Finding that the vertical aspects of the acquisition were neither "of monopoly nor _de minimus_ proportions," the Court said that the percentage of the market that was foreclosed could not be in itself decisive. But the evidence showed that Brown would use the acquisition "to force Brown shoes into Kinney stores." There was a trend toward vertical integration in the industry, in which the acquiring manufacturers had increasingly become sources of supply for their acquired outlets, and "the necessary corollary of these trends is the foreclosure of independent manufacturers from markets otherwise open to them." Brown was the fourth largest manufacturer and Kinney, the acquired firm, the largest independent chain of family shoe stores. Thus "no merger between a manufacturer and an independent retailer could involve a larger potential market foreclosure." Though Brown argued that there were many manufacturers and retailers and that competition was dynamically competitive, "remaining vigor cannot immunize a merger if the trend in that industry is toward oligopoly." The law forbade the merger "because the trend toward vertical integration in the shoe industry, when combined with Brown's avowed policy of forcing its own shoes upon its retail subsidiaries, may foreclose competition from a substantial share of the market for men's, women's, and children's shoes, without producing any countervailing competitive, economic, or social advantages."

The broadest attack upon vertical mergers has been that in the cement industry, against mergers by which cement manufacturers acquired firms that produce ready-mixed concrete. Though in 1960 there was almost no vertical integration of such operations, by the close of 1965 leading

cement firms had acquired at least 40 producers of that product (which accounted for about three fourths of all cement), and several large producers of ready-mixed concrete had begun to make cement.[38] From 1960 to 1965 the Federal Trade Commission issued 10 complaints against instances of forward vertical integration in the industry.[39] In 1964 the Commission directed its economic staff to make an industry-wide investigation. It published the resulting report in 1966, held a public hearing about the problem later that year, and in January 1967, issued a policy statement about such mergers.[40] The following summary is based upon that statement and the underlying report; the quotations are from the statement.

The industrial setting, as seen by the Commission, was one in which, because of transportation cost, each urban market typically was served by few cement producers and by few producers of ready-mixed concrete, often with substantial concentration in such markets. In metropolitan markets ready-mixed concrete firms were dominant consumers of cement, and hence "the crucial link in cement distribution and use." A merger uniting the two types of firm in a metropolitan area was likely to result in objectionable foreclosure, induce others to merge, impair competition by the unintegrated, and raise barriers to entry.

"When one or more major ready-mixed concrete firms are tied through ownership to particular cement suppliers, the resulting foreclosure not only may be significant in the short run, but may impose heavy long-run burdens on the disadvantaged cement suppliers who continue selling in markets affected by integration. Acquisitions of leading cement consumers in markets containing comparatively few volume buyers may have the effect of substantially disrupting the competitive situation at the cement level, and, in fact, may set off a

'chain' reaction of acquisitions."

"Unintegrated ready-mixed concrete producers furthermore may be at a disadvantage in competing with rivals who are integrated cement and concrete manufacturers. This is true not only because of disparities in size and access to capital, and the advantages inherent in product and market diversification, but also because of the potential 'price squeeze' latent in competition with integrated companies."

"The more extensive vertical integration becomes in the cement and concrete industries, the higher tends to be the level of entry barriers in individual metropolitan markets and in larger geographic regions. This can result from a number of causes. Higher capital requirements are necessitated by entry into the production of cement and ready-mixed concrete on an integrated basis. The capital requirements for entry on an integrated basis appear to be double the cost of entry into the production of cement only. But the need for far more capital is not the only problem. Industry executives at the public hearings were unanimous in stating the difficulty of penetrating the ready-mixed concrete industry on a significant scale in markets containing long-established ready-mixed concrete producers. New entrants in ready-mixed concrete in integrated markets, of course, may face the additional deterring effect of competition with very large, diversified and integrated rivals."

On the basis of this analysis, the Commission decided "to investigate expeditiously every future acquisition by a cement producer of any substantial ready-mixed concrete firm in any market to which such acquiring producer is an actual or potential supplier." Except in unusual circumstances, it said, it would regard as substantial an acquisition of any of the

leading four non-integrated producers of ready-mixed concrete in any metropolitan market, or of any other consumer of cement that regularly bought annually 50,000 barrels of cement or more.

It considered equivalent to such an acquisition a series of acquisitions of several smaller ready-mixed concrete producers with about the same cumulative purchases, or any acquisition that, with the forward integration previously attained, gave the cement producer a position equivalent to the size specified. As to markets where integration had already occurred, the statement said that, since partly integrated markets may still attract new cement producers and new producers of ready-mixed concrete, the Commission intended "to act to preserve the open portions of partially integrated markets to the fullest extent possible."

The statement was supplemented by a declaration that in some markets acquisition of key producers of aggregates (e.g., sand and gravel) can become means of pressure upon cement consumers, and that therefore the Commission would "oppose the acquisition of key aggregates suppliers in a market wherever there is reason to believe that such acquisitions may confer upon the acquiring cement company any significant ability to exert anticompetitive 'leverage' on cement consumers affecting their freedom to choose cement suppliers."

Finally, the Commission said (with two dissents) that it would require all portland cement companies to notify it at least 60 days before acquiring any producer of ready-mixed concrete, and for this purpose would use the power to require reports given it by Section 6 of the Federal Trade Commission Act.

The part of the policy statement by the Department of Justice that pertains to vertical mergers endeavours to integrate and make generally applicable the types of appraisal evident in the Brown decision and the Commission's statement about cement.[41] It describes as follows the competitive problems that vertical mergers may involve:

"Barriers to entry resting on such factors as economies of scale in production and distribution are not questionable as such. But vertical mergers tend to raise barriers to entry in undesirable ways, particularly the following: 1) by foreclosing equal access to potential customers, thus reducing the ability of non-integrated firms to capture competitively the market share needed to achieve an efficient level of production, or imposing the burden of entry on an integrated basis (i.e., at both the supplying and purchasing levels) even though entry at a single level would permit efficient operation; 11) by foreclosing equal access to potential suppliers, thus either increasing the risk of a price or supply squeeze on the new entrant or imposing the additional burden of entry as an integrated firm; or 111) by facilitating promotional product differentiation when the merger involves a manufacturing firm's acquisition of firms at the retail level. Besides impeding the entry of new sellers, the foregoing consequences of vertical mergers, if present, also artificially inhibit the expansion of presently competing sellers by conferring on the merged firm competitive advantages, unrelated to real economies of production or distribution, over non-integrated or partly integrated firms. While it is true that in some instances vertical integration may raise barriers to entry or disadvantage existing competitors only as the result of the achievement of significant economies of production or distribution (as, for example, where the increase

in barriers is due to achievement of economies of integrated production through an alteration of the structure of the plant as well as of the firm) integration accomplished by a large vertical merger will usually raise entry barriers or disadvantage competitors to an extent not accounted for by, and wholly disproportionate to, such economies as may result from the merger."

Admitting that circumstances that produce such effects are difficult to identify with precision, the guidelines state the Department's belief that "the market shares of the merging firms and the conditions of entry which already exist in the relevant markets;...will ordinarily serve to identify most of the situations in which any of the various possible adverse effects of vertical mergers may occur and be of substantial competitive significance." At the market level of the supplying firm, the statement says, vertical acquisitions will be challenged if the supplying firm makes 10 per cent or more of sales in its market and mergers with one or more firms that make, in all, six per cent or more of total purchases in that market, unless it is clear that there are no significant barriers to entry by more purchasers.

Though intervention where there are these percentages would meet many of the problems that arise in markets served by the purchasing firm, the statement says, some problems remain: mergers may, at the purchasing firm's level, raise barriers to entry or disadvantage that firm's competitors "by conferring upon the purchasing firm a significant competitive advantage over unintegrated, or partly integrated, existing competitors or over potential competitors." Such advantages are thought probable when, because of a shortage of supply or a temporary superiority of the product supplied by the integrated supplier, competitors

of the integrated purchaser are subjected to a supply squeeze by the integrated supplier's refusal to sell to them or to a price squeeze by reduction of the margin between the supplier's price to them and the purchaser's price for the end product, or when would-be entrants are confronted by risk of such a squeeze. The Department says that to cope with such a problem it will ordinarily challenge mergers by a supplier with 20 per cent more of sales in its market and one or more purchasers with an aggregate of 10 per cent or more of sales in the market for the product into which the purchased supply is made. That these percentages are larger than those used in challenges based upon effects in the market of the supplying firm is presumably due to belief that squeezes in the market of the purchasing firm are possible only when there is control of relatively large market shares.

As in the case of horizontal mergers, the Department supplements the standards that rest upon percentages of relevant markets by additional ones that have other bases. The cases considered "most common" pertain to the trend of vertical integration. Challenge can ordinarily be anticipated, the Department says, for vertical acquisitions by "major firms" in industries in which, "(1), there has been or is developing, a significant trend toward vertical integration by merger such that the trend, if unchallenged, would probably raise barriers to entry or impose a competitive disadvantage on unintegrated or partly integrated firms, and (2), it does not clearly appear that the particular acquisition will result in significant economies of production or distribution unrelated to advertising or other promotional economies." Unlike the similar standard for horizontal mergers, however, the standard here makes no attempt to express its purpose in

percentages.

The other standard specifically mentioned is that of restrictive purpose, which the Department thinks "less common." The focus is upon acquisitions "for the purpose of increasing the difficulty of potential competitors in entering the market of either the acquiring or acquired firm, or for the purpose of putting competitors of either the acquiring or acquired firm at an unwarranted disadvantage."

As in the case of horizontal mergers, the guidelines provide for exemption of failing companies, with the same reservation about the scope of the exemption.

Though, as in the case of horizontal mergers, rejection of claims of economy as justification of challenged mergers is asserted, the substance of the rejection is much further qualified. It not only states, like the previous one, that it applies "unless there are exceptional circumstances," it also refers specifically to absence of proof of significant economies as one of the conditions for challenge of mergers that contribute to a trend toward vertical integration. Moreover, the statement of grounds for challenge of vertical mergers believed to have adverse effects on competition includes recognition that in some instances barriers to entry and disadvantage to competitors might develop only as a result of economies. Nevertheless, the statement says that substantial economies "can normally" be realized by internal expansion, and that when barriers to entry by such expansion are encountered, the standards for challenge usually will involve no challenge "to the acquisition of a firm or firms of sufficient size to overcome or adequately minimize the barriers to entry."

Potential competition. The questions that arise when a merger unites a corporation that is in a market with one that might be so resemble those relevant to a horizontal merger. A firm that might have become a competitor ceases to have that role, and thus the potential for future competition is diminished in a degree that depends upon the kind and extent of the competitive role that this potentiality involved.

Mergers of this type fall into two subclasses. In one, the competitive aspect of the potential competition consists of the probability that, but for the merger, entry by the potential competitor would take place, and competition would be thereby intensified. In particular instances, the entry that the merger has foreclosed may be conceived as construction of appropriate facilities by the entrant's internal expansion; in other instances, as the entrant's acquisition of a small facility in the market - a so-called "toe-hold" acquisition - that the entrant then would have expanded into an operation of significant size. A merger can foreclose entry in either of these ways.

In the other class of potential entries, the competitive aspect consists of the continuing ability of a potential entrant that does not enter the market to do so if incentives to do so are increased by developments there, e.g., by rising prices and profits--an ability that enduringly exposes enterprises there to quasi-competitive pressures upon their conduct. A merger that unites the potential entrant with an enterprise already there removes that kind of pressure.

A case against El Paso Natural Gas Company illustrates both aspects of potential competi-

tion in a setting or expansion of territorial markets.[42] El Paso was the only supplier of natural gas to California markets from sources outside the state. It acquired the assets of Pacific Northwest Pipeline Company (the only other interstate supplier of natural gas on the West Coast), which was then supplying nearby states, had not succeeded in past efforts to enter California, but was able to build the necessary pipeline. The Supreme Court held that the size of the California market, and Pacific Northwest's nearness to it and eagerness to enter it, created a strong likelihood that the entry would have occurred; and that past unsuccessful efforts by Pacific Northwest had had "a powerful influence on El Paso's business attitudes." The Court held that the acquisition was unlawful and must be divested, on the ground that it tended to maintain a monopoly by El Paso.

The concept of a potential entrant involves degrees of potentiality that are difficult to express in policy. The most logical entrants into a market presumably are firms that possess some of the relevant facilities and expertise appropriate to operation there and have experience in markets in which problems are similar. But as resources have become more widely available and experts have become more numerous and more mobile, there has been more opportunity for a firm to acquire them if it has access to enough money. Thus it has become increasingly difficult to appraise the likelihood that a particular firm will enter a particular market, and still more difficult to appraise the strength of belief among firms in that market that a particular firm or one of several firms may do so. A firm with enough resources is, in a sense, a potential entrant to all markets from which the law does not exclude it. Nevertheless, firms usually do not contemplate entering a market with which

they have no familiarity, unless they have formulated concepts of their own future that include the market as a "natural" field for expansion. To know the content of such corporate self-images is hard, and to decide what weight to give to them is still harder.

Thus, though the centre of the concept of potential competition may be clear, its boundaries blur off into speculative uncertainty. No definition of it in one industrial context is likely to be reliable in another, and no consensus as to its scope has been attained.

In the light of these difficulties, the effort to cope with it in the statement of merger guidelines by the Department of Justice is worth noting. Concerned about the "most likely" entrants, the Department defines these as follows: "...the Department accords primary significance to the firm's capability of entering on a competitively significant scale relative to the capability of other firms (i.e., the technological and financial resources available to it) and to the firm's economic incentive to enter (evidenced by, for example, the general attractiveness of the market in terms of risk and profit; or any special relationship of the firm to the market; or the firm's manifested interest in entry; or the natural expansion pattern of the firm; or the like)."[43]

The Department says that it will ordinarily challenge a merger that involves one of such entrants and a) any firm with 25 per cent or more of the market; b) either of the two largest firms in the market if they together have 50 per cent or more of it; c) any of the four largest, if the largest eight have 75 per cent or more and the one merging has 10 per cent or more; d) and any one of the eight largest if they

together have 75 per cent or more and if either the merging firm's share of the market is growing rapidly or that firm's share is "not insubstantial" and there are only one or two likely entrants. It also says that it will challenge any merger with a likely entrant if the purpose is to prevent competitive "disturbance" or "disruption."

Without attempting to define potential competitors, the Federal Trade Commission discusses them in a policy statement for grocery manufacturing.[44] On the basis of recent experience, it says, the large grocery manufacturers are the leading potential entrants into most grocery product markets; they have entered almost exclusively by acquiring leading independent firms; though many of the larger firms have the capacity to enter, few of them at any one time have a strong incentive to do so; and not more than 50 of the 30,000 food manufacturers are the leading potential entrants into highly concentrated grocery product industries.

Joint Ventures. Closely related to potential competition are the acquisitions by which parts of the assets of two or more enterprises are combined in a jointly-owned firm that undertakes activity of a specialized kind. In many instances the incentive for the joint venture is that none of the participants possesses singly the range of assets and skills that is needed for full effectiveness in the undertaking. Under such conditions the immediate effect of the joint venture may be to initiate activity that otherwise would not be begun or that, if done alone, would be less efficient. Where this is clearly so, there is no need for antitrust intervention.

But another possibility is that participants in the joint venture may each be well able to enter the field singly, but choose to

avoid the competition that would ensue by entering collaboratively, so that neither confronts the other as either an active or a potential competitor. The collaboration may also make entry by other potential entrants more difficult. Moreover, if joint ventures were exempt under the law as to mergers, it would not be difficult to give the form of a joint venture to various acquisitions that are substantively anticompetitive.

The status of joint ventures under Section 7 was settled by the Penn-Olin case.[45] Pennsalt, a manufacturer of sodium chlorate in Portland, Oregon, had nearly 58 per cent of the sodium chlorate sales west of the Rocky Mountains. Two larger manufacturers of the product controlled more than 90 per cent of the expanding market in the southeast. Pennsalt had considered and rejected four plans to build a plant there. Olin-Mathieson, a large chemical company, had also considered entry into the southeastern market. After successful experiment with an arrangement in which Olin-Mathieson, as sales agent for Pennsalt, made nearly nine per cent of southeastern sales, the two companies formed a joint venture in 1960, Penn-Olin, with a new plant in Kentucky. By 1962 Penn-Olin had nearly 28 per cent of the market. The Department of Justice then sued under Section 7. The Supreme Court decided in 1964 that Section 7 is applicable to joint ventures, and that the same legal considerations apply to such ventures as to mergers. Whereas the district court had held that the venture would be illegal only if both parties would otherwise have entered the market, the Supreme Court held that if the merger would have prevented either from entering alone while the other remained a potential competitor the venture would be unlawful; and after reviewing the record the Court concluded that "unless we are going to require subjective evidence, this array of probability certainly reaches the

prima facie stage." The case was returned to the lower court on remand. However, that court decided that the Government had not proved that either firm would have entered independently. Thus the applicable law has been decided except as to the kind of proof needed to show the probability of entry. There has been so little relevant subsequent litigation that the Supreme Court has not yet had occasion to settle the dispute touched off by the decision between those who say that such evidence should be "subjective" and those who say that it should be "objective."

Impact of a Merger Upon Business Concentration

Actions about horizontal mergers and mergers with potential competitors, such as have been summarized above, have been focussed upon particular relevant markets, with the purpose of preventing mergers from creating monopolies or oligopolies there. Similarly, action about vertical mergers has been focussed upon preservation of competition in the relationships between particular markets. Policies toward the types of merger discussed below have focus broader than particular markets. These policies have developed from belief that business concentration is growing in the economy as a whole, that this growth is anticompetitive in tendency, that mergers have contributed significantly to it, and that, unlike growth of firms by other means, growth by merger seldom makes significant contributions to efficiency and progress that could not be attained by other means.[46] Increase in vertical integration and in horizontal diversification, and development of oligopolies in particular markets, are seen as manifestations of a general trend to reduce the number of relatively small firms and increase the part of the economy controlled by a few big ones. The purpose of merger policy, thus seen, is both to prevent particular anticompetitive

changes in particular markets and to retard or reverse the general concentrative tendency.

When a merger is examined from this point of view, market shares are not the chief points of attention. Relevant aspects of mergers are the size of the firm after the merger, the magnitude of the acquisition, the number of acquisitions by the same acquirer, the decrease in the number of firms operating in a segment of the economy, the effect of change in the size of the merged enterprise upon relations between it and firms with which it competes or deals, and the impact of changes in the size and number of existing firms upon entry into business by new firms and upon entry into new markets by existing ones.

<u>Mergers that Extend Territorial Markets</u>. The point of view just summarized first became prominent for mergers that united firms in different territorial markets in analysis of industries that produced dairy products and that distributed food. In both fields, local independent firms were being rapidly absorbed into large national chains. The industry's business units were becoming fewer and larger. In each industry, many local markets were being changed into oligopolies, and the identity of the oligopolists was the same in many localities. In the dairy industry, products such as cheese and butter, which had wide markets, were becoming regionally or nationally oligopolized. In food distribution, various types of discriminatory use of bargaining power had become important enough to result in drastic revision of the laws applicable to price discrimination.

The Federal Trade Commission interpreted these developments as symptoms of growing concentration throughout these industries. It formulated the concept of market extension, and began to take action against such mergers. In

the dairy industry, a series of proceedings against the largest companies reduced their growth by merger, without much hindrance to mergers among smaller dairies.[47] In food distribution, the Commission undertook a series of merger cases against large chains -- National Tea,[48] Kroger,[49] Grand Union,[50] Consolidated Foods,[51] and Winn-Dixie.[52]

The National Tea case, the first of these, illustrates such proceedings. The firm was charged with violating both Section 7 and Section 5 of the Federal Trade Commission Act. Fifth largest chain in size, it had acquired 485 grocery stores, of which 450 were located in areas in which it had not operated before the acquisition. The proceeding challenged 13 of these acquisitions that had been made between 1952 and 1958. The Commission did not analyze the local markets involved nor focus upon the acquirer's market share there. Instead, it held that such acquisitions by so large a company were prima facie unlawful. The record in the case seemed to the Commission to show "that the large multi-market character of firms of this size may give them substantial advantages over smaller firms, and that some of these advantages are entirely unrelated to economic efficiency."[53] The order in the case did not require divestiture, but required that for a period of 10 years the company acquire no retail food store without prior approval by the Commission.

When the Commission spoke about merger policy in these industries, it emphasized size of firm and the trend of concentration. The statement about food distribution began by saying that the industry "has become increasingly concentrated in both national and local markets," and that the growth in concentration "has been caused in significant part, and certainly accelerated, by a nationwide merger movement among large super-

market chains."[54] Though many of these developments were "in response to normal and desirable market forces, others might bring about unnecessary and irreversible changes inimical to the market structure and competitive behavior of food retailing."

Similarly, the statement about dairy mergers, after saying that orders by the Commission had stopped merger activity by the four largest dairies, noted a "threat of renewed merger activity ruinous to competition in the dairy industry," and said "a resumption of leading firm market extension mergers would again threaten the preservation of a strong middle tier of independent dairies. The preservation of this tier of viable independent companies is essential to the competitive health of the dairy industry."[55]

Accordingly, the Commission has announced criteria for action in these industries that stress size instead of market share. In food distribution it considers that legal attention is warranted for a) "mergers and acquisitions by retail food chains which result in combined annual food store sales in excess of $500 million annually"; and b) "mergers and acquisitions by voluntary and cooperative groups of food retailers creating a wholesale volume of sales comparable to those of food chains with sales in excess of $500 million annually." Though market-extension mergers by companies with smaller sales "generally do not pose a serious threat to competition except when they involve some competitive overlap," the policy includes determination whether there is a legal problem in "mergers and acquisitions by food chains or wholesalers which result in combined annual food store sales of between $100 million and $500 million."

However, the Commission thinks that ordinarily it need not review a) a merger of "not more than four food or grocery stores"; b) a merger of stores or wholesaling establishments "representing annual food or grocery product sales of not more than $5 million" and c) a merger of such stores or establishments "representing combined food store sales of not more than five per cent of total food store sales in any city or county in the United States."

The criteria for dairy mergers emphasize the size of dairy firms as shown by the number of pounds of Class 1 milk that they process. The Commission will "focus particular attention" upon acquisitions in which the acquirer processes more than one billion pounds annually. It will investigate acquisitions with focus upon two points, the number of pounds processed by the acquired and the distance of what is acquired from the acquirer. Presumably this distance is regarded as a rough indication of the potentiality of competition by the acquired. The Commission will investigate if the acquired processes 300 million pounds annually, regardless of its distance, and if the acquired is within a 150 mile radius from the acquirer, regardless of its size. For smaller amounts and greater distances, both variables are considered, in ways specified.

This statement of policy contains the only detailed market-share criteria that the Commission has used. It consists in adaptation for the dairy industry of percentages of the market formulated in the guidelines of the Department of Justice. The context indicates, however, that the Commission will use these percentages as shares of regional or adjacent markets, not local ones.

Since the types of anticompetitive effect that have been attributed to multimarket size from territorial mergers are similar to those that have been attributed to such size when it results from product extension mergers or from mergers of unrelated activities and judicial consideration of them has come primarily in cases involving product-extention mergers, the status of market-extension mergers at law will not be separately discussed.

Mergers That Extend Product Lines. Exploration of the concept of product-extension mergers was also first undertaken by the Federal Trade Commission. Such a merger is one in which a firm adds to its line of products, not by constructing whatever facilities are needed to produce the new product and developing whatever skills are needed to produce and market it, but by acquiring another firm that has done this. As in considering mergers for market extension, the Commission has been concerned about such acquisitions chiefly when the acquirer is large and the acquired is substantially smaller.

That Section 7 can be used against product-extension mergers became clear in 1967 in the Supreme Court's decision in the Procter & Gamble case.[56] Clorox, the leading manufacturer of liquid bleach, had been acquired by Procter & Gamble, a much larger diversified manufacturer that had a dominant position in several related fields but had not made liquid bleach. Reversing the circuit court, the Supreme Court condemned the merger in a way similar to that of the Federal Trade Commission's original decision against it. Section 7 covers all mergers, said the Court, and all mergers "must be tested by the same standard, whether they are horizontal, vertical, conglomerate, or other." Impairment of competition by the

acquisition of Clorox was probable for several reasons. Procter had been the most probable of the few potential entrants into production and sale of liquid bleach. Since all liquid bleach is chemically identical, success in selling it depended largely on effectiveness in sales promotion. The acquisition had strengthened Clorox against other firms in the market in that it had made available to Clorox the discounts on advertising expenditures that Procter was receiving (by which the same expenditures would now give Clorox the benefit of about one third more advertising), and had made available also the services of Procter's strong sales organization. Moreover, being diversified and financially strong, Procter was able to reduce prices on liquid bleach if it wished, an ability that might reduce competition "by dissuading the smaller firms from aggressively competing" because of "their fear of retaliation by Procter." The additional strength that the merger, and the consequent support by Procter, had given to Clorox had raised the barriers to entry into the market by other potential competitors.

One important consideration about product-extension mergers that was not relevant to the Procter & Gamble case, the possible effect of such mergers in encouraging reciprocity, had already been condemned in another case, in which the Commission had challenged an acquisition by Consolidated Foods.[57] Gentry, one of two major sources of dehydrated onion and garlic, had been acquired by Consolidated, a large distributor of processed food products. The challenge rested on the probability that food processors would buy their dehydrated onion and garlic from Gentry as an inducement for Consolidated to buy processed foods from them. Reversing the circuit court, the Supreme Court held that reciprocity "'results in an irrelevant

and alien factor' intruding into the choice among competing products, creating at least 'a priority on the business at equal prices.'" Finding that the merger had altered the market by creating a situation conducive to reciprocity, the Court concluded that substantial lessening of competition was reasonably probable.

Since that decision, doubts about the status of reciprocity at law have been focussed upon the nature of the requisite proof of the existence and the substantiality of the relationship. To use reciprocity systematically as a weapon in selling, a large diversified corporation needs to compile the amounts of its purchases in such a way that totals for various kinds of purchases from various sources are computed as aggregates from each supplier, and that these aggregates become available to its sales staff. If reciprocity with other large firms is important to it, it may designate an official to specialize in reciprocity negotiations. Investigation easily discovers evidence of such activities; and where the evidence is found, legal liability attaches not only to mergers that enhance the chance of using reciprocity, but also, under Section 1 of the Sherman Act and Section 5 of the Federal Trade Commission Act, to reciprocity agreements that restrain trade. The difficult question about reciprocity in mergers is whether anything more is needed than proof that the changes in business structure made by the merger have somewhat increased the advantage of making some purchases from firms to which some sales could be made. As a court of appeals said in 1963, "The mere existence of this purchasing power might make its conscious employment toward this end unnecessary; the possession of the power is frequently sufficient, as sophisticated businessmen are quick to see the advantages in securing the good will of the possessor."[58]

With its position supported by the Supreme Court decisions in the Consolidated Foods and Procter & Gamble cases, the Federal Trade Commission issued in May 1968, a policy statement about product-extension mergers by manufacturers of grocery products.[59] The statement rested explicitly upon concern about changes in the structure of this part of the economy, and found support in a recent report by the National Commission on Food Marketing. It began, "The market structure of the grocery products manufacturing sector of the economy has changed significantly in recent years. Small companies are tending to disappear, diversification and conglomeration are becoming more extensive, and market concentration has been increasing in many grocery product markets. Large-scale promotional activity and heavy advertising expenditures by the largest food manufacturing companies have both resulted from and contributed to these structural changes. The National Commission on Food Marketing concluded on the basis of its exhaustive study that food manufacturing firms 'tend to grow, especially by merger and acquisition, well beyond the size needed to attain full operating efficiency'. It further called for 'positive action by the regulatory agencies' to make the Clayton Act merger policy effective."

The Commission's concern was summarized in statistics to the effect that the decline in the number of food manufacturers had been such that, if the rate continued, the number would be halved by 1985; in 1966 the 50 largest firms had 52 per cent of all the assets of all food manufacturers, as compared with 42 per cent in 1950, and these 50 received in 1967 about 61 per cent of the total profits of them all; more than 20 per cent of all food industries were very highly concentrated oligopolies, and about 10 per cent more were concentrated though to lesser degrees; in 1964, the largest 50 were responsible for 88 per cent of all network television advertising and 78 per

cent of all advertising in general magazines.

Partly in quotations from the final report by the National Commission on Food Marketing and partly in its own statements, the Commission said that high concentration weakens competition as a self-regulating device; tends to substitute competition by advertising and sales promotion for price competition; fosters diversification that enables large firms to survive their own mistakes, compete intensively in selected fields, and make arrangements for reciprocity, and adversely affects conditions of entry.

Product-extension mergers, the Commission said, had been in food manufacturing a "tide", with mergers concentrated among the largest firms. Acquisitions of firms that had sales of $10 million or more had eliminated since 1950 a total of 80 such firms, and in 1966 only 219 firms of that size were left. The 50 firms largest in 1965 had obtained by merger since 1951 almost one fourth of their total assets and almost 40 per cent of their growth in assets.

The Commission said that its criterion for opposing a product-extension merger would be a) that both of the firms involved were manufacturers of grocery products; b) that the assets when combined were over $250 million; c) that the acquiring firm engages in extensive promotional efforts, sells highly differentiated consumer products, and produces a number of products, in some of which it holds a strong market position (with such a position defined as being among the top four producers of a product of which the four hold 40 per cent or more of the value of shipments, and d) that the acquired firm is either among the top eight producers of one important product or has more than five per cent of a relevant market.

Though the Department of Justice did not accept all of the Commission's analysis, its merger guidelines, issued in the same month as the statement about food manufacturing, gave general application to two segments of the same point of view.[60]

Calling reciprocity an economically unjustified practice that gives advantage unrelated to the merits of the product, the Department expressed intention to challenge "any merger which creates a significant danger of reciprocal buying." It considered that, apart from special factors, a significant danger "is present whenever approximately 15 per cent or more of the total purchases in a market in which one of the firms ('the selling firm') sells are accounted for by firms which also make substantial sales in markets where the other merging firm ('the buying firm') is both a substantial buyer and a more substantial buyer than all or most of the competitors of the selling firm." I said that it will also challenge mergers undertaken for the purpose of facilitating reciprocity, and mergers that create the possibility of it where one or both of the merging firms has engaged in the practice recently or the merged firm is doing so. It will not regard claims of economy as a justification.

The other part of the guidelines that is relevant pertains to "entrenchment". The Department so defines the term as to include much that concerned the Commission in its statement about grocery products, but treats it, not as ground for challenge of the merger but as ground for investigation. The Department says that it will investigate the possibility of anticompetitive consequences "where an acquisition of a leading firm in a relatively concentrated or rapidly concentrating market may serve to entrench or increase the market power of that firm or raise barriers to entry in that market."

It gives three examples: "i) a merger which produces a large disparity in absolute size between the merged firm and the largest firms remaining in the relevant markets; ii) a merger of firms producing related products which may induce purchasers, concerned about the merged firm's possible use of leverage, to buy products of the merged firm rather than those of competitors; and iii) a merger which may enhance the ability of the merged firm to increase product differentiation in the relevant markets."

Conglomerate Mergers. The objectives and criteria for action of the Commission's statement about grocery products focus upon concentration and bigness in a way that can be extended readily to conglomerate mergers - that is, to mergers that unite firms engaged in unrelated activities. Mergers across industry lines can increase the absolute size of merged firms; be a source of advantage in advertising and sales promotion; enlarge opportunities for reciprocity; eliminate potential competitors; reduce the total number of firms, and induce smaller firms to compete more cautiously for fear of the financial strength of their larger rivals and the ability of these rivals to reduce prices with little difficulty in selected segments of their total business. From the formulation for grocery products to a policy against conglomerate mergers was a short extension.

In 1968 this extension was made in a policy statement by the Commission about mergers as to textile mill products. The statement was applicable to all four kinds of mergers that the Commission had previously identified - horizontal, vertical, market-extension, and product-extension. The objectives of policy were stated with appropriate breadth: "to arrest anticompetitive or monopolistic tendencies in their incipient

stages by challenging: horizontal mergers which may substantially increase market concentration; vertical mergers which may substantially foreclose access to sources of supply or markets or raise entry barriers; and product- or market-extension mergers which may raise entry barriers, create reciprocity opportunities, or eliminate the constraints potential entrants place upon firms in the market without any of the pro-competitive effects of internal entry. Thus, in its enforcement guides the Commission endeavors... 1) to forestall anticompetitive tendencies by directing merger activity away from areas where it may increase concentration, and at the same time 2) to promote entry by internal investment which creates new capacity and additional competitive rivalry among firms."

The criteria for assessing mergers that the Commission then applied included not only ones similar to those of previous statements but also a new one, applicable to mergers between industries. The Commission thought that "significant questions of law or policy" would need to be examined as to "any acquisition of a textile mill product firm with sales or assets of $100 million or more and ranking among the four largest producers of a textile mill product by a non-textile mill product firm with sales or assets in excess of $250 million and with a substantial market position in another industry." It defined a substantial market position as being "one of the top four sellers of a product or service in which the four largest companies account for 40 per cent or more of the market." Thus it stated concern about large conglomerate mergers that absorb large textile firms.

The extension aroused controversy. Commissioner Jones dissented, thinking that the statement had outrun the supporting evidence. The industry urged that the statement be withdrawn or revised, emphasizing objection to the

part about mergers across the industry line. A year later the Commission reaffirmed the policy, with dissents by Commissioners Jones and MacIntyre. The dissent by the latter objected to the use of dollar amounts instead of percentages within the textile industry and focused sharply upon the criterion about inter-industry mergers, finding it, not wrong in principle, but too rigourous in content: "no such merger has been found by the Commission or any court to be violative of the law. However...I am of the view that perhaps such merger could be challenged successfully if it could be shown that it was creating an enormous super concentration of economic power and such fact could be looked to as probably giving rise to a showing of substantial adverse effects across industry lines. The representatives of the Textile Industry have expressed the view that a firm of a size of $100 million is not of such size. I am inclined to agree, and for that reason, I think the Commission was in error in taking the contrary view."[61]

The guidelines issued in 1968 by the Department of Justice were cautious in discussing conglomerate mergers. Treating as conglomerate all mergers that are not horizontal or vertical, they set forth policies (summarized above) about potential competition, reciprocity, and entrenchment. They then said that the conglomerate merger field involves novel problems that need continuous analysis to identify anti-competitive effects, and mentioned as an instance action "to prevent mergers which may diminish long-run possibilities of enhanced competition resulting from technological developments that may increase inter-product competition between industries whose products are presently relatively imperfect substitute." Presumably this example reflects continued reluctance to apply policy except with focus upon effects in particular markets.

This reluctance soon ceased. In the latter part of the 1960's, conglomerate mergers had been growing in number and size and had become significant concentrative influences upon the economy as a whole. In March 1969, a new Assistant Attorney General testified before a Congressional committee that "predecessors at the Antitrust Division took the position that purer forms of conglomerate merger could not be reached under Section 7 because in their view, where merging firms are commercially unrelated, proof cannot generally be made of a reasonable likelihood of a substantial lessening of competition...businessmen and their lawyers cannot rely on the merger guidelines issued by my predecessors in this regard... we are willing to risk losing some cases to find out how far Section 7 will take us in halting the current accelerated trend toward concentration by merger."[62] In June the Attorney General said in a speech that the Department "may very well" oppose any merger among the top 200 manufacturing firms or firms of comparable size in other industries, and probably would oppose a merger of such a firm with any leading producer in any concentrated industry.[63]

Underlying this change of position was a substantial controversy over policy. Substantively it has not been resolved[64] though its public manifestations and immediate significance have been much reduced by the fact that large conglomerates, hard hit by recent economic developments, are currently undertaking very few mergers.

Under the new policy, the Department of Justice began to challenge large conglomerate mergers. It attacked acquisitions by three companies - Northwest Industries for its attempt to acquire Goodrich; Ling-Temco-Vought for its

acquisition of Jones & Laughlin, and International Telephone and Telegraph for acquisition of three important firms. The case against Ling-Temco-Vought shows the nature of the attacks. In April 1969, it asked for divestiture of a controlling stock interest that LTV had acquired in Jones & Laughlin Steel Corporation.[65] Ling, the nation's fourteenth largest industrial firm, had acquired control of 33 companies since 1961 and was planning further acquisitions. At the time of the suit, according to the complaint, it was, through operating subsidiaries, the largest seller of sporting goods, the third largest meat packer, the third largest car-rental firm, the seventh largest commercial airline, one of the largest manufacturers of copper wire, and a major producer of sound equipment, electronic controls, chemicals, aircraft parts, aerospace equipment, jet fighter planes, and carpeting. Jones & Laughlin, the sixth largest producer of steel, had sales of more than $1 billion in 1968, assets of more than $1.15 billion, and ranked eightieth in the nation among industrial firms in assets and one hundredth in sales. It had adopted in 1967 a program of acquisition and diversification.

The anticompetitive effects attributed to the merger were stated in language appropriate to any merger involving diversified firms comparably large: "a) Potential independent competition by LTV and J&L Steel may be diminished in the steel industry, in other markets in which only one of them presently competes, and in certain other markets in which neither of them presently competes; b) the power of LTV and J&L Steel, and of their suppliers, to employ and to benefit from reciprocity and reciprocity effects in the sale of their products will be substantially enhanced, and the markets for their competitors' goods will be correspondingly narrowed; c) concentration of control of manufacturing assets

will be substantially increased, and the trend to further concentration by merger will be encouraged, thereby I) reducing the number of firms capable of entering concentrated markets; II) reducing the number of firms with the capability and incentive for competitive innovation; III) increasing the barriers to entry in concentrated markets; and IV) diminishing the vigor of competition by increasing actual and potential customer-supplier relationships among leading firms in concentrated markets."

Judicial review to determine the validity of such an application of Section 7 has not yet taken place. The case resulted in a consent decree in June 1970 by which LTV was to divest itself of its ownership of J&L or alternatively of its ownership of Braniff Airways and of Okonite, a producer of insulated wire and cable.[66]

The other major challenge, which involved acquisitions by International Telephone and Telegraph Corp., has also been settled by consent, amid a controversy that developed into an aspect of that politico-economic upheaval now called "Watergate".[67] The case involving Northwest Industries and Goodrich was dismissed without predjudice on May 3, 1974 on the Government's motion.[68]

Though the controversy about policy toward conglomerate mergers is now quiescent, it probably will become lively again when the economic climate stimulates more large mergers of this kind. If Section 7 proves adequate to cope with it, policy probably will emerge from decisions in litigated cases. If the decisions hold that Section 7 does not cover such mergers, a political issue about them presumably will come to focus and eventually be settled by legislative decision.

In November 1972, the Commission made public a study by its economic staff which attempted to provide a firmer basis for appraisal of the conflict over policy toward conglomerate mergers.[69] This study was based upon "in-depth questionnaires" to nine leading conglomerate firms. It said that 88 per cent of the mergers by these nine had been conglomerate, and that in 1968 the nine accounted for 26 per cent of the assets of all firms acquired and 45 per cent of the assets acquired in unrelated conglomerate mergers. It reported that the acquired firms, for the most part, were profitable and growing, though with rates of return slightly below their industry averages. In general, the acquisitions had been in industries in which concentration was less than in the industries in which the acquirers were already engaged. The acquirers apparently did not acquire substantial market positions in the new areas; in 82 per cent of the acquired product classes, these firms had market shares of less than five per cent. From the times of the acquisitions until 1969, market shares showed declines more often than increases. There was no evidence that the acquirers had made many improvements in the operations of the acquired firms; the data contained no evidence of "corporate synergism." The clearest effect of the acquisitions had been to obscure information relevant to the performance of firms, since the acquirers do not publish operating results by product lines. The effect appeared to be an "informational barrier to entry," and a possibility that lack of industry profit data might hamper the efficient operation of markets dominated by those firms.

The Impact of the Law.

Enforcement of Section 7 clearly has not stopped mergers, though it may have retarded them and probably has deflected some of them

into fields where they are less subject to challenge. The latest summary information is contained in a report by the Commission for the year 1973 and earlier.[70] It indicates that in 1973, a total of 1,919 mergers were completed in all branches of the economy, with more than 900 pending. Of those completed, 753 were by acquirers with assets of $100 million or more, and another 208 by acquirers with assets of more than $50 million. Though 1,782 of the firms acquired had assets of less than $10 million, 147 of them were larger, including 41 with assets of more than $50 million, of which 28 had assets of more than $100 million. The 55 acquisitions in manufacturing and mining that were among those in which the acquired had assets of $10 million or more included 13 that were horizontal, seven that were vertical, 10 that were for product extension, six that were for market extension, and 19 others (presumably truly conglomerate). These 55 acquisitions involved total acquired assets of nearly $2,900 million, of which more than 40 per cent were acquired by the 200 largest firms.

These large acquisitions (those in which the acquired had $10 million or more) increased in number and in aggregate assets acquired from the time Section 7 was amended until 1955; fluctuated around the levels then reached until 1967; rose sharply in 1968 to a peak of 173 acquisitions involving aggregate acquired assets of more than $12,500 million, and then receded quickly to about the 1973 level.

VII - MERGERS

Footnotes

1. Earl W. Kintner, Primer on the Law of Mergers, Macmillan Co., New York, 1973, p.192.

2. As to acquisitions of stock, the law exempts them if made solely for investment and not used by voting or otherwise in attempts to reduce competition. Also exempt is ownership of stock by a corporate parent in subsidiaries formed by it. Though there is no similar statutory language about partial acquisitions of assets, the fact that illegality depends upon the probability that competition will be reduced means in practice that such acquisitions are almost never vulnerable except when what is acquired is an entire productive facility or an important patent or trademark. In this essay, partial acquisitions will be ignored except where they are sufficiently important to be treated as mergers.

3. Kintner, op. cit., pp. 162-164. The cases were: U.S. v. Northern Securities Co., 193 US 197 (1904); U.S. v. Union Pacific Railroad, 226 US 61 (1912); U.S. v. Reading Co., 253 U.S. 26 (1920); U.S. v. Southern Pacific Co., 259 U.S. 214 (1922).

4. U.S. v. Columbia Steel Co., 334 US 495 (1948).

5. The statutory phrase "where the effect... may be" was interpreted by the Supreme Court in Standard Fashion Co. v. Magrane-Houston Co., 258 US 346 (1922), to mean reasonable probability, not mere possibility. With one unimportant aberration,

this meaning has been consistently applied to "may be" in Clayton Act cases.

6. The 1914 text was as follows: "That no corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of another corporation engaged also in commerce where the effect of such acquisition may be to substantially lessen competition between the corporation whose stock is so acquired and the corporation making the acquisition or to restrain such commerce in any section or community or tend to create a monopoly of any line of commerce. No corporation shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of two or more corporations engaged in commerce where the effect of such acquisition or the use of such stock by the voting or granting of proxies or otherwise may be to substantially lessen competition between such corporations, or any of them, whose stock or other share capital is so acquired, or to restrain such commerce in any section or community or tend to create a monopoly of any line of commerce."

7. In F.T.C. v. Western Meat Co., 272 US 554 (1926), the Supreme Court held that Western could not acquire assets instead of stock after the Commission had issued an order against the stock acquisition, since this would be evasion of the Commission's order. In Thatcher Manufacturing Co. v. F.T.C., 272 US 554 (1926), it held that when the asset acquisition was completed before the Commission's complaint against the stock acquisition, the former was immune to the Commission's order. In Arrow-Hart & Hegeman Electric Co. v. F.T.C., 63 F. 2d. 108

(2d Circuit, 1933), reversed 291 US 587 (1934). The Supreme Court extended the rule of the Thatcher case by immunizing an asset acquisition made during the Commission's proceeding against the prior stock acquisition.

8. In International Shoe Co. v. F.T.C., 280 US 291 (1930), the Supreme Court held that: "Mere acquisition by one corporation of the stock of a competitor, even though it results in some lessening of competition, is not forbidden; the act deals only with such acquisitions as probably will result in lessening competition to a substantial degree...that is to say, to such a degree as will injuriously affect the public. Obviously, such acquisition will not produce the forbidden results if there be no pre-existing substantial competition to be affected; for the public is not concerned in the lessening of competition which... is itself without real substance."

9. In 1949, a charge under Section 7 was added to a complaint under the Sherman Act against the relationship between General Motors and DuPont. Deciding this proceeding under the old version of Section 7, but after the new version had been enacted, the Supreme Court held in 1957 that the vertical acquisition was illegal. See U.S. v. E.I. duPont de Nemours & Co., 353 US 586 (1957).

10. Congressional interest was stimulated by a Federal Trade Commission report in 1948, that during the period 1940-1947, corporate mergers had eliminated nearly 2,500 firms with aggregate assets of $5 billion -- 5.5 per cent of all United States manufacturing

assets. See the Federal Trade Commission, <u>The Merger Movement, a Summary Report</u>, 1948.

11. A principal purpose of the limitation was to define as to Section 7 the limits of the function of the Federal Trade Commission in making decisions under that Section in relation to the functions of other agencies that, in applying that section in accord with their jurisdiction under Section 11 of the Act, would need to relate it to various degrees of power over acquisitions of stock, assets, or both, that they possessed under various regulatory statutes. An effort to cope with the status of asset acquisitions in the light of these various regulatory statutes would have required consideration of the problem by more than one committee in each of the houses of Congress, and probably would have jeopardized enactment of the amendment during the session of Congress in which it was enacted. The effect of the limitation was to leave unchanged the status of asset acquisitions under the various regulatory laws, but to extend Section 7 to cover asset acquisitions in the large segment of the economy over which the Federal Trade Commission has jurisdiction.

The limitation did not affect the legality of acquisitions of either stock or assets under the Sherman Act, nor the right of the Department of Justice to proceed in the courts against violations under Section 15 of the Clayton Act to enforce both the Sherman Act and the Clayton Act if either was violated.

The principal problem that subsequently arose pertained to the status of bank

mergers. In U.S. v. Philadelphia National Bank, 374 US 321 (1963), the Supreme Court applied Section 7 in declaring illegal a proposed consolidation of two Philadelphia banks. It found that a merger of banks was not neatly an acquisition of either stock or assets, but that the intention of Congress had been to reach "the entire range of corporate amalgamations" and that the special laws about banking did not exempt bank mergers from the antitrust laws nor empower the regulatory authorities to do so. Controversy over this decision resulted in 1966 in amendment of the Bank Merger Act. The new version made conclusively lawful all mergers by banks prior to the decision in the Philadelphia Bank case if these had not yet been challenged, except those that violated Section 2 of the Sherman Act (the section about monopolization). Mergers in pending cases were to be subjected to the standards of the amendment. In considering new mergers, the banking authorities were forbidden to approve mergers that violated the standards of the Sherman Act, and required, as to mergers that would have violated the standards of Section 7, to approve them only if the anticompetitive effects of the merger were "clearly outweighed" by its beneficial effects upon the public interest. Bank mergers that were approved by the banking authorities were to be stayed for 30 days, during which the Department of Justice could bring about a further stay by suit under the antitrust laws; in such a suit the courts were instructed to review the issues de novo. After termination of the suit or failure to institute it during the time period, the merger was to be immune from other antitrust challenge except under Section 2

of the Sherman Act. (See Kintner, op.cit., note 1, pp. 425-429, for a summary of the legislation).

The effect of the new law upon the standards applied in the Philadelphia Bank case was decided by the Supreme Court in U.S. v. First National Bank of Houston and U.S. v. Provident National Bank, 386 US 361 (1967), and U.S. v. Third National Bank in Nashville, 390 U.S. 171 (1968). In the first two cases the Court unanimously decided favourably to the Department of Justice, several issues about the nature of pleading, the burden of proof, and the scope of judicial review. In the third, overruling the district court, it held that the standards of the Philadelphia decision were still valid in appraising anticompetitive effects, and that the first step in deciding whether or not there were over-riding public benefits must be that the trial court "sufficiently or reliably establish the unavailability of alternate solutions" of the problems that the merger was claimed to have solved. Only by applying the standards of the Philadelphia case and considering whether or not the banks involved had tried without success to solve their problems could the courts validly decide whether or not benefits outweighed anticompetitive effects.

Thus decisions in the Philadelphia case and cases subsequent to the one against the Nashville bank are relevant, so far as anticompetitive effects are concerned, in appraising the meaning of Section 7 in non-banking fields. An example of such a decision is U.S. v. Philipsburg National Bank, 399 US 350 (1970). For a discussion of the evolu-

tion of policy toward bank mergers, see Kintner, _op. cit._, note 1, pp. 411-448.

12. House Report No. 1191, 81st Congress, 1st session, 1949; Senate Report No. 1775, 81st Congress, 2nd session, 1950.

13. F.T.C. v. Motion Picture Advertising Service Co., Inc., 344 US 392 (1953); F.T.C. v. Brown Shoe Co., Inc., 384 US 316 (1966).

14. U.S. v. E.I. duPont de Nemours & Co., _op. cit._, note 9.

15. Department of Justice Merger Guidelines, issued May 1968, reprinted in Kintner, _op. cit._, note 1, pp 506-515, at 508.

16. _Ibid_, at p. 507.

17. The Supreme Court answered the question affirmatively in U.S. v. E.I. duPont de Nemours & Co., _op. cit._, note 9.

18. The Supreme Court thought such further division unnecessary in Brown Shoe Co. v. U.S., 370 US 294 (1962).

19. Reversing the circuit court, the Supreme Court found the two types of container reasonably interchangeable and thus parts of a single line in U.S. v. Continental Can Co., 378 US 441 (1964).

20. This issue was explored in Brown Shoe v. U.S., _op. cit._, note 18.

21. This question was decided in U.S. v. Philadelphia National Bank, _op. cit._, note 11. Though this case involved banking, the decision began by ruling that the law applicable to non-financial

enterprises was also applicable to the case. Thus the decision is pertinent to the meaning of Section 7 in the cases discussed here.

22. Brown Shoe v. U.S., _op. cit._, note 18. The concept of sub-markets had been previously elaborated in a case that did not reach the Supreme Court: U.S. v. Bethleham Steel Corp., 168 F. Supp. 576 (S.D.N.Y., 1958).

23. U.S. v. Philadelphia National Bank, _op. cit._, note 11: "The proper question to be asked in this case is not where the parties to the merger do business or even where they compete, but where, in the area of competitive overlap, the effect of the merger on competition will be direct and immediate."

24. _Ibid_.

25. In U.S. v. Pabst Brewing Co., 384 US 546 (1966), the Supreme Court expressed impatience with meticulous requirements for market definition. It said that the law "requires merely that the Government prove the merger may have a substantial anticompetitive effect somewhere in the United States -- in _any_ section of the United States. This phrase does not call for the delineation of a section of the country by metes and bounds as a survevor would lay off a plot of ground ... Congress did not seem to be troubled about the exact spot where competition might be lessened; it simply intended to outlaw mergers which threatened competition in any or all parts of the country. Proof of the section of the country where the anticompetitive effect exists is entirely subsidiary to the crucial question in

this and every Section 7 case which is whether a merger may substantially lessen competition anywhere in the United States."

26. Department of Justice Merger Guidelines, op. cit., note 15, Kintner, op. cit., note 1, p. 507.

27. At that time I was the Commission's chief economist. Eventually the Commission's decision against Pillsbury was set aside by the Fifth Circuit on the ground that a committee of the Congress had intruded improperly into the process of adjudication. The Commission then dismissed the case. See the Commission's annual report for 1966, p. 72.

28. In one early proceeding, a defendant argued that proof of the validity of a table of figures required that the government produce all documents in which figures entering into the compilation were originally entered, and make available for examination each person responsible for the resulting compilation. The table was short, but the government contended that the documents would have filled a freight car and that questioning of the compilers would have required a week. Though the demand was obviously extravagent, it indicates the general nature of the problem that must be solved in using official statistics.

29. Shortly after I left the Federal Trade Commission's staff, after I had made a speech to an economics seminar, I was asked what I could suggest as a way of getting more economics into merger cases. I replied that to my mind the need was for a way to get into them less economics

yet attain reasonably satisfactory decisions. The economist who at that time was the Commission's recognized expert on merger problems was in the audience, and agreed vigourously. As to the problem of developing suitable rules of thumb for mergers, see Derek C. Bok, "Section 7 of the Clayton Act and the Merging of Law and Economics", Harvard Law Review, December 1960, p. 226.

30. Requirements by the Commission for prior report of mergers began with the cement industry and the food distribution industry in 1967. In 1969 the requirement was made general for all manufacturing corporations subject to the Commission's jurisdiction as to large mergers. As in effect in 1974, the general requirement called for notice of acquisitions of manufacturing companies with sales or assets of more than $10 million where the combined sales or assets exceeded $250 million, and notice of acquisitions of non-manufacturing companies where the assets exceeded these figures. The requirement also covered tender offers.

31. Department of Justice Merger Guidelines, op. cit., note 15.

32. In 1973 the Commission was given power to seek injunctive relief in the district courts by amendments to the Federal Trade Commission Act included in legislation authorizing the Alaskan Pipeline; see James T. Halverson, Director, Bureau of Competition of the Federal Trade Commission, The FTC's Plans for Use of the Injunctive Powers Granted to it in the Alaskan Pipeline Bill, speech to the FTC Compliance Institute, New York, New York, May 17, 1974 (mimeographed).

33. U.S. v. Philadelphia National Bank, _op. cit_., note 11.

34. Luria Brothers Co., 62 FTC 243 (1963). As to the breadth of the Commission's power to issue orders, see Atlantic Richfield Co. v. F.T.C., 381 US 357 (1965), though this was not a merger case. See also F.T.C. v. Rubberoid, 343 US 470 (1952).

35. U.S. v. Von's Grocery Co., 384 US 270 (1966).

36. Department of Justice Merger Guidelines, _op. cit_., note 15, at p. 508.

37. Brown Shoe Co. v. U.S., _op. cit_., note 18.

38. Staff Report to the Federal Trade Commission, _Economic Report on Mergers and Vertical Integration In the Cement Industry_, April 1966, p. 1.

39. _Ibid_., pp. 3-5. Some of the acquisitions were of concrete pipe producers and producers of aggregates. During the period, two complaints also involved horizontal mergers by cement companies.

40. Enforcement Policy with Respect to Vertical Mergers in the Cement Industry, released January 17, 1967; see CCH, 1971 Trade Regulation Reports, #4520.

41. Department of Justice Merger Guidelines, _op. cit_., note 15, at p. 510.

42. U.S. v. El Paso Natural Gas Co., 376 US 651 (1964).

43. Justice Department Merger Guidelines, _op. cit_., note 15, at p. 514.

44. Enforcement Policy with Respect to Product Extension Mergers in Grocery Products Manufacturing, released May 15, 1968; see CCH, 1971 Trade Regulation Reports, #4530.

45. U.S. v. Penn-Olin Chemical Co., 378 US 158 (1964).

46. For a recent statement of this point of view, see Corwin D. Edwards, "Policy Toward Big Business: What Lessons After Forty Years?", 9 Journal of Economic Issues 343, June 1975. For an earlier statement, see Corwin D. Edwards "Conglomerate Bigness as a Source of Power," in National Bureau of Economic Research, Business Concentration and Price Policy, 1955, p. 331.

47. Important decisions pertained to Foremost Dairies, 60 FTC 944 (1962), order modified 67 FTC 282 (1965); National Dairy Products Corp., 62 FTC 120 (1963); Borden Co., 65 FTC 296 (1964) and Beatrice Foods Co., 67 FTC 473 (1965).

Though use of the market extension concept in merger cases began in the 1950's, the Department of Justice has done little with it except in proceedings against bank mergers, and had little success in such proceedings. From the Supreme Court's Philadelphia National Bank decision, (see note 11), until mid-1972, five bank merger cases were lost by the Department, all of them involving market extension. They pertained to Crocker-Anglo National Bank, First National Bank of Jackson, Bank of Maryland, Bank of Jackson, Idaho First National, and Bank of Greeley. The Greeley merger reached the Supreme Court in 1973, but the district court's decision remained in effect, without opinion by the Supreme Court, when the latter divided four to

four. (See U.S. v. First National Bancorporation, 329 F. Supp. 1003 (D. Colo., 1971), affirmed by an equally divided court, 410 US 577 (1973)). Informants at the Department of Justice tell me that even more recent decisions about market-extension mergers by banks have been lost by the Government.

Judicial decisions in such cases appear to be affected by the fact that under current procedures bank mergers have taken place only after the responsible authority has found that benefits from them outweigh anticompetitive effects. Though the courts have repeatedly condemned bank mergers in spite of such prior approval, they apparently have been reluctant to do so when the grounds for challenge were not direct effect but the less direct ones anticipated from market extension.

48. National Tea Co., 69 FTC 226 (1966). The order was not appealed.

49. Docket 7464, complaint April 1, 1959. The case was terminated by the Commission October 31, 1968, after the relevant policy about the industry had been issued and the case had become nearly 10 years old.

50. Docket 8458, complaint Jan. 12, 1962. This case pertained to acquisition of direct competitors. It was settled June 10, 1965, by a consent order that required divestiture of certain supermarkets and forbade the company for 10 years to acquire competitors larger than a stated size without the Commission's prior approval.

51. Docket C-1024. The firm had acquired three grocery chains. On Dec. 21, 1965, a consent order required that stores with combined sales of more than $200 million be divested, and prohibited further acquisitions of grocery stores and dairy product stores without prior approval by the Commission.

52. Docket C-1110. This case was settled by consent. No divestiture was ordered, but further acquisitions were banned for 10 years. The ban was subsequently modified to apply only to horizontal market-extension mergers.

53. Enforcement policy with Respect to Mergers in Food Distribution Industries, news release Jan. 17, 1969; see CCH, 1971 Trade Regulation Reports #4525.

54. Ibid.

55. Enforcement Policy with Respect to Mergers in the Dairy Industry, July 2, 1973; see CCH, 1971 Trade Regulation Reports Paragraph 4532.

56. F.T.C. v. Procter & Gamble Company, 386 US 568 (1967). The Commission's case was Docket 6901, and the decision appears in 63 FTC 1465 (1963).

57. F.T.C.v. Consolidated Foods Corp., 380 US 592 (1965).

58. U.S.v. Ingersoll-Rand Co., 320 F. 2d. 509 (3rd Circuit, 1963).

59. Enforcement Policy with Respect to Product Extention Mergers in Grocery Products Manufacturing, released May 15, 1969; see

CCH, 1971 Trade Regulation Reports #4530. This statement quotes frequently from Food from Farmer to Consumer, Final Report of the National Commission on Food Marketing, June 1966, and from that commission's Technical Study No. 8, The Structure of Food Manufacturing.

60. Department of Justice Merger Guidelines, op. cit., note 15, at 514-515.

61. The original statement, Enforcement Policy with Respect to Mergers in the Textile Mill Products Industry, issued Nov. 22, 1968, appears with the reaffirmation of Aug. 18, 1969, and the dissents to both statements in CCH, 1971 Trade Regulation Reports, #4535.

62. Statement by Richard MacLaren at Hearings on H.R. 13,270 before Committee On Ways and Means of the House of Representatives, 91st Congress, 1st session, part 7, at 2389 (1969).

63. Address by Attorney General John Mitchell to the Georgia Bar Association, Savannah, Georgia, June 6, 1969; see 115 Congressional Record 6480 (daily edition)June 16, 1969.

64. There has been controversy both about the recent importance of conglomerate mergers in economic concentration and about the appropriate content of the law as to such mergers. As to the underlying facts, see Bureau of Economics, Federal Trade Commission, Economic Report on Corporate Mergers, 1969; also articles in St. John's Law Review, Spring 1960, special edition, by Stanley E. Boyle, p. 152 and Raymond Puscini, p. 171; also Betty Bock and Jack Farkas, Relative Growth of the 'Largest'

Manufacturing Corporations, 1947-1971: Subsets from an Unknown Set, New York, Conference Board, 1973. For two views of appropriate policy, see 1968 White House Task Force Report on Antitrust Policy (the Neal Report), 115 Congressional Record 5651 (daily edition) May 27, 1969, and White House Task Force Report on Productivity and Competition (the Stigler Report) 115 Congressional Record 647 (daily ed) June 16, 1969. See also in the cited issue of the St. John's Law Review the articles by Joel B. Dirlam, p. 193; Mary Gardiner Jones and Edward J. Heiden, p. 243; Corwin D. Edwards, p. 416; Richard A. Soloman, p. 559; John Vanderstar, p. 596; John T. Miller, p. 613; Luther C. McKinney, p. 635; Robert H. Bork, p. 663; William L. McGovern, p. 655; and Betty Bock p. 694. See also Corwin D. Edwards "Economic Concepts and Antitrust Litigation: Evolving Complexities," 19 Antitrust Bulletin 295, and Corwin D. Edwards "The Significance of Conglomerate Concentration in Modern Economies," in Helmut Arndt (ed.) Die Konzentration in der Wirtschaft (Berlin, Duncker & Humblot, 1971) vol. 2, p. 137.

65. U.S. v. Ling-Temco-Vought, Jones & Laughlin Steel Corp., and Jones & Laughlin Industries, Inc., Civil action No. 69-438; see CCH, 1970 Trade Cases #73228.

66. See CCH, 1970, trade cases #73105.

67. Three acquisitions by ITT were challenged in three separate cases. These involved acquisition of Canteen Corporation, a leading vending-machine organization with 1968 revenues of $322 million; Grinnell (268th in rank in Fortune Magazine's list of the 500 largest manufacturing corpora-

tions), the largest producer and installer of automatic sprinkler fire protection systems, with 1968 sales of $341 million; and Hartford Fire Insurance Co., fourth among the nation's property and liability insurance firms, with premium receipts in 1968 of nearly $1 billion. The Antitrust Division, initially eager to press the Hartford and Grinnell cases to a judicial decision, accepted in June 1971 a consent settlement which allowed ITT to keep Hartford, but required it to divest its interests in Canteen and part of Grinnell, also required it to divest its holdings in Avis, a large car-rental company, and in Levitt, the largest construction enterprise, and prohibited it from acquiring any corporation with assets of $100 million or more without prior approval. The process by which the settlement was reached is described in Anthony Sampson, The Sovereign State of ITT, chapter 7, and the subsequent reverberations in his chapters 8-10.

68. Civ. 69-C1102, N.D. Illinois, May 3, 1974.

69. Staff Report to the Federal Trade Commission, Conglomerate Merger Performance, an Empirical Analysis of Nine Corporations, November 1972. The nine firms were ITT, LTV, Litton Industries, Gulf and Western Industries, Textron, FMC Corporation, Rapid American Corporation, Norton Simon, Inc., and White Consolidated Industries.

70. Federal Trade Commission Bureau of Economics, Statistical Report on Mergers and Acquisitions, July 1974. The figures given in the text are taken from pages 15-16, 143, 147-148, and 151.

V111 - MONOPOLIZATION

Since 1890, Section 2 of the Sherman Act has forbidden monopolization. It provides that "every person who shall monopolize or attempt to monopolize, or combine or conspire with any other person or persons to monopolize, any part of the trade or commerce among the several states, or with foreign nations, shall be deemed guilty of a misdemeanor." The provision can be enforced by fine, imprisonment, or judicial decree, or a combination of these; and under Section 4 of the Clayton Act, private persons injured by the offense can recover three times the amount of the damage.

Any one of three types of action is subject to this provision: monopolization by a single offender; an attempt to monopolize by a single offender, even if unsuccessful; and participation in a joint effort to monopolize, whether or not successful, by any party to a combination or conspiracy. Each of these types of action has been held to be a separate offense, so that a defendant may be guilty of more than one of them; and instances of such multiple guilt are sometimes alleged and found.[1]

Conspiracy to Monopolize.

Conspiracy cases under Section 2 (like such cases under Section 1) do not involve need to demonstrate the size of a relevant market and the magnitude of the share of that market possessed by defendants, as is usually necessary in proving monopolization.[2] Where conspiracy to monopolize can be shown, therefore, it sometimes makes the case simpler to frame the charge as conspiracy. In cases thus framed, the allegations pertain to activity in which what is charged under Section 2 would also be a violation

of Section 1. Section 1 of the Act forbids "every contract, combination in the form of trust or otherwise, or conspiracy" that restrains trade. Though not every combination or conspiracy to restrain trade is necessarily one to monopolize, every one that monopolizes a part of commerce obviously restrains trade. The key case against Standard Oil Company of New Jersey that first broadly interpreted Section 2 resulted in convictions under both Section 2 and Section 1; the Supreme Court's decision blended both sections and emphasized their relationship: "Having by the first section forbidden all means of monopolizing trade, that is, unduly restraining it by means of every contract, combination, etc., the second section seeks, if possible, to make the prohibitions of the Act all the more complete and perfect by embracing all attempts to reach the end prohibited by the first section..."[3]

The close connection between the two sections means, in practice, that seldom if ever can anything more be achieved by the Government by convicting defendants of combination or conspiracy to monopolize than by convicting them of an offense that is smaller and more easily proved, agreement to restrain trade. In this essay I shall disregard the conspiracy cases under Section 2. The significance of this part of the law lies in its other two aspects, monopolization and attempt to monopolize.

Monopolization.

Monopolization obviously means something more than sole occupancy of an industry or market; for obviously the law does not mean that the innovator who establishes a new industry or the last surviving firm in a dying industry shall be deemed a monopolist. Some further element is needed to convert occupancy

of most or all of the field into monopolization. In the Standard Oil decision the judicial conception of this element was "unification of power," which was said to give rise "to the prima facie presumption of intent and purpose to maintain the dominancy over the oil industry," and conduct by the parties, which included various unconscionable acts, was found to have confirmed the presumption conclusively. Nine years later, in acquitting United States Steel, the Court held, "The corporation is undoubtedly of impressive size...But...the law does not make mere size an offense, or the existence of unexerted power an offense. It...requires overt acts, trusts to its prohibition of them and its power to repress or punish them."[4] As to such acts, the Court held, "whatever there was of wrong intent could not be executed, whatever there was of evil effect was discontinued before this suit was brought."

Considered together, these decisions defined the law of monopolization for the next 25 years. The offense consisted of possession of power and restrictive use of it. Restrictive conduct by the powerful firm was evidence of unlawful intent, and a firm's ability to engage in such conduct without aid by others was evidence of possession of power. The chief significant modification of this view was a decision that, though mere size is not enough to constitute an offense, when magnified to the point at which it gives monopoly, "size carries with it an opportunity for abuse that is not to be ignored when the opportunity is proved to have been utilized in the past."[5] Thus the offense consisted of power and unlawful intent, but the latter was to be found in present or past misconduct. In effect, Section 2 was applicable to powerful enterprises that misbehaved, but not to ones that behaved properly.

This interpretation was revised in the decision against the Aluminum Company of America

(Alcoa) in 1945.[6] Alcoa was found to possess a monopoly because it had a monopolistic percentage of the market for aluminum ingot. Though Alcoa was the only domestic producer of such ingot, its percentage of the supply could be computed differently, from 33 per cent to more than 90 per cent, depending upon whether or not the computation included ingot that Alcoa itself used in further fabrication, imported ingot that had been produced in Canada by a subsidiary, imported ingot originating with other companies, and "secondary" (that is, reprocessed) ingot. The extent of the inclusion was important, because the court held that the highest percentage clearly meant monopoly, whereas monopoly with 60 per cent or 64 per cent was doubtful, and 33 per cent was certainly insufficient. After extended analysis, the court concluded that the percentage was more than 90. It held that so large a share meant "complete control", within limits set by incentives not to raise prices so high as to incur excessive costs of idle capacity or as to bring in more uncontrolled supply.

The legal importance of the distinction between good and bad conduct was explicitly repudiated: monopolizing is not excused if "the monopoly has not been used to extract from the consumer more than a 'fair' profit"; for such a profit might be made at lower prices. There were possibilities that "possession of unchallenged economic power deadens initiative, discourages thrift, and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone.. ...that competitors, versed in the craft as no consumer can be, will be quick to detect opportunities for saving and new shifts in production, and be eager to profit by them." Though the law might have been formulated to

condemn only monopolies that were deficient in such respects, "Congress...did not condone 'good trusts' and condemn 'bad' ones; it forbade all. Moreover, in so doing, it was not necessarily actuated by economic motives alone. It is possible, because of its indirect social or moral effect, to prefer a system of small producers, each dependent for his success upon his own skill and character, to one in which the great mass of those engaged must accept the direction of a few. These considerations, which we have suggested only as possible purposes of the Act, we think the decisions prove to have been in fact its purposes...Throughout the history of these statutes it has been constantly assumed that one of their purposes was to perpetuate and preserve, for its own sake and in spite of possible cost, an organization of industry in small units which can effectively compete with each other. We hold that 'Alcoa's' monopoly was of the kind covered by Section 2."

But the court thought that monopoly was not inevitably unlawful. "This notion has usually been expressed by saying that size does not determine guilt; that there must be some 'exclusion' of competitors; that the growth must be something else than 'natural' or 'normal'; that there must be a 'wrongful intent' or some other specific intent; or that some 'unduly' coercive means must be used....What engendered these compunctions is reasonably plain; persons may find themselves in possession of a monopoly...without having intended either to put an end to existing competition, or to prevent competition from arising when none had existed....Since the Act makes 'monopolizing' a crime, as well as a civil wrong, it would be not only unfair, but presumably contrary to the intent of Congress, to include such instances. A market may, for example, be so limited that

it is impossible to produce at all and meet the cost of production except by a plant large enough to supply the whole demand. Or there may be changes in taste or in cost which drive out all but one purveyor. A single producer may be the survivor out of a group of active competitors, merely by virtue of his superior skill, foresight, and industry. In such cases a strong argument can be made that, although the result may expose the public to the evils of monopoly, the Act does not mean to condemn the resultant of those very forces which it is its prime object to foster...The successful competitor, having been urged to compete, must not be turned upon when he wins."

Alcoa, however, was not "the passive beneficiary of a monopoly." It had acted to maintain its own power. In demonstrating this fact, the opinion was careful to emphasize conduct by Alcoa that, in itself, is not reprehensible and in less powerful firms could be commendable. "It was not inevitable that it should always anticipate increases in the demand for ingot and be prepared to supply them. Nothing compelled it to keep doubling and redoubling its capacity before others entered the field. It insists that it never excluded competitors; but we can think of no more effective exclusion than progressively to embrace each new opportunity as it opened, and to face every newcomer with new capacity already geared into a great organization, having the advantage of experience, trade connections and the elite of personnel. Only in case we interpret 'exclusion' as limited to manoeuvres not honestly industrial, but actuated solely by a desire to prevent competition, can such a course, indefatigably pursued, be deemed not 'exclusionary'. So to limit it would in our judgment emasculate the Act; would permit just such consolidations as it was designed to prevent."

With such an analysis, intend had been attenuated. Though it was important as to conduct that fell short of monopoly, in a case in which monopoly existed "no monopolist monopolizes unconscious of what he is doing... 'Alcoa' meant to keep, and did keep, that complete and exclusive hold upon the ingot market with which it started. That was to 'monopolize' that market, however innocently it otherwise proceeded."

Since this decision, nation-wide monopolization cases have needed to involve only two central questions: 1) is the defendant's place in the market sufficiently large to be monopoly? 2) if so, has the defendant done anything to attain or maintain that place that was not inherent in the process of doing business? The requisite control is manifested by possession of a share of the market that approaches total occupancy,[7] or, where the share is too small to be conclusive, from conduct by the enterprise that would be foolish or impossible if control was not possessed. Thus conduct remains important as proof of monopoly chiefly in considering cases that are near the border-line. The requisite purpose to get or keep control consists of any activity not unavoidable that had the effect of creating, maintaining, or extending the control. Neither proof of specific purpose to monopolize nor proof of reprehensible conduct is needed to establish the Government's case. The meaning of the law has become, in effect, that all avoidable monopolies shall be prevented.

Monopoly thrust upon the monopolist by environmental circumstances or by his "skill, industry, and foresight" has appeared chiefly in such instances as monopoly of local exhibition of motion pictures in a community too small to support more than one theatre and too isolated for inter-community competition

by such exhibitors. Such a monopoly is lawful; but might become vulnerable if, as the community grew larger, the possessor of it were to prevent entry by a second exhibitor by purchasing the best available vacant lot. Ordinarily a monopoly that is neither deliberately sought nor deliberately maintained is not prosecuted. Occasionally, a case is begun but the defendant wins on such grounds.[8]

The full extent to which the second central question precludes activity by a monopoly that would be deemed innocent if done by others has not yet become clear. The case against Alcoa condemned monopoly by persistent expansion of facilities. In a subsequent case against the largest maker of shoe machinery, the chief reason for condemning a firm that supplied between 75 per cent and 85 per cent of the national market and had attained this position lawfully was that its dominant position had been maintained by a policy of leasing the machinery instead of selling it.[9] No case, so far as I am aware, has yet been focussed upon the question whether or not persistently large and successful expenditures for technological research by a monopoly would be similarly condemned.

In monopolization cases, as in cases about mergers, definition of the relevant market may be a significant issue. The "part" of commerce that must not be monopolized was defined in the Standard Oil decision: it "includes any portion of the United States and any one of the classes of things forming a part of interstate and foreign commerce."[10] As to national monopolies, the territorial aspect of definition of the market raises occasional difficulty where there is uncertainty whether imported supplies should be considered as being outside or within the market. Definition of the extent of

the market as to commodities or services may raise difficulty wherever the commerce controlled by the large firm is not neatly co-extensive with the scope of a recognized industry. In the Grinnell case, for example, the decision against Grinnell turned upon the question whether different kinds of systems for protection of property from fire and theft should be regarded as in different markets or, as the Supreme Court decided, a cluster of such systems operated from central stations should be regarded as a single market; and if the latter, whether the market included only systems accredited by insurance companies or also systems not thus accredited.[11] In the cellophane case, DuPont was acquitted because the Supreme Court held that the relevant market was not that for cellophane, which DuPont clearly controlled, but that for flexible wrapping materials, of which DuPont provided less than 18 per cent.[12] Thus decisions about the scope of the market are sometimes decisive in cases national in breadth. As will appear below, definition of the market grows in importance where the market is not national.

A pending case against International Business Machines is at present the largest, most complex, and most important Governmental attack upon monopolization. It is the culmination of several earlier and smaller proceedings, public and private. In 1932, the Government charged that IBM and Remington-Rand had monopolized tablutaling machines and tabulating cards by agreement. Before trial the agreements were cancelled, and in 1935 certain restrictions in machine leases were adjudged illegal.[13] Another Government suit in 1952, charging that IBM monopolized the tabulating machine industry, ended in a consent judgment in 1956.[14] A cross-licensing agreement between Sperry-Rand and IBM about patents and know-how as to

electronic data processing, which the 1956 decree did not cover, resulted in a suit by Honeywell against Sperry-Rand in 1967, based on the contention that the agreement was a technological merger, and in a decision in 1973 invalidating relevant patents.[15] Smaller producers of electric data processing equipment sued IBM for damages. Suit by one, Greyhound, was dismissed in 1972, with findings that the evidence, though insufficient, indicated that IBM's monopoly resulted from superior skill, foresight, and industry, and that no evidence had shown attempt to monopolize.[16] Suit by another, Control Data, was settled by agreement in 1973.[17] Suit by a third, Telex, resulted in decision that the relevant market was that for peripheral electronic data products that were plug compatible to IBM central processing units and that IBM had willfully monopolized that market. About $260 million was awarded to Telex, and IBM was enjoined from specified conduct.[18] Various otherprivate suits were pending in 1969, at the time of the Government's complaint.

The present complaint, as to which trial is just beginning, charges that IBM has attempted to monopolize and has monopolized commerce in general purpose digital computers.[19] IBM is described as the largest manufacturer of information handling equipment in the world, with 1967 total revenues of more than $5.3 billion, total assets of nearly $5.6 billion, and net income of $651 million. Its challenged activities, as specified, are: a) use of a pricing policy by which a single price covers hardware, software, and related support, with discrimination among customers in software, and with effects of inhibited entry and growth by competitors, and of limiting the development and scope of independent

software and support industries; b) use of software and related support to preclude competitors from competing effectively for various accounts; c) introduction of computers with unusually low profit expectations in segments of the market where competitors had or appeared likely to have unusual success, and announcing future production of new models for such markets when it knew that it was not likely to produce them in the announced time; d) domination of the educational market by granting discriminatory allowances to universities and other educational institutions. The Government has tentatively asked for separation of IBM into several "discreet, separate, independent, and competitively balanced entities"; for supplementary orders designed to give these entities access to know-how and equipment; for interim orders to forbid IBM from marketing its systems by "bundled prices"; pricing parts of its systems at predatory prices or discriminatory ones, and announcing new products before making them is feasible.

Monopolization cases recurrently involve unusual difficulties in framing judicial decrees. Where unlawful monopoly power is found to arise from particular types of conduct not inherent in doing business - e.g., tying agreements - termination of it by decree is no more difficult than in most antitrust cases. Where a decree requires a defendant to perform a series of acts through an appreciable time period in accord with some standard set by the decree, the court sometimes must perform quasi-administrative duties in policing the decree. The greatest difficulties arise, however, where termination of monopoly power is possible only by dissolution of a well-integrated monopolist. In such cases, competition will be effectively restored only if each part into which the monopolist is broken is a viable enterprise, capable of sustaining itself against the others. If such firms are to be created by judicial decree, the court often needs information, much of which is not needed in determining that there has been violation, and needs

an expertise broader than that obtainable from legal training. If, for example, the IBM case should end in an order of dissolution, the decree will reshape the computer industry thoughout the world and substantially change many aspects of the developing use of computers in private and public affairs.

Aware of the breadth of their responsibility, courts tend so to limit their orders as to be confident that they know what they are doing. In consequence, dissolution decrees tend to under-correct the conditions to which they are addressed.

Foreseeing this type of difficulty, Congress tried to provide a way of meeting it in 1914 in the Federal Trade Commission Act. Section 7 of that Act authorizes courts that desire to grant relief in equity proceedings by the Attorney General to refer the suit to the Commission as a master in chancery "to ascertain and report an appropriate form of decree therein," but provides that the court may "accept or reject such report, in whole or in part." This effort to use the Commission's presumed expertise and unusually broad powers to get information has had substantially no results. In practice, courts do not make such references. Apparently a judge who has immersed himself in a difficult case is willing neither to entrust the issues to study de novo by an outside body, however expert, nor to incur the additional delay in termination of a long proceeding that necessarily would result from such a reference.

Since enactment of the Sherman Act, and partly as a result of that Act, large companies usually have developed in the United States

not as national monopolies but as oligopolies or as firms diversified across several industries. Unless there is conspiracy among such companies, the concept of monopoly does not fit well a situation of shared power. In an oligopoly, competition by the large companies with one another may be significantly diverted from price competition to rivalry in advertising and selling and to innovative changes, whether or not functionally useful in the characteristics of goods. Though the influence of each big company is attenuated by the presence of others, and cannot readily be called control, yet it may be so large that small competitors are intimidated by their own awareness of what their big rival might do to them. They accept its initiative and acquiesce in its decisions about prices, methods of marketing, and the characteristics of products, thus becoming docile conformists instead of active competitors.[20]

Efforts to cope with such anticompetitive developments by use of Section 2 have been made, and have been partly successful. Where an oligopolist has a dominant place in a segregable part of an industry, that part may be defined as a sub-market, and his preponderance there may be defined as monopolization of it, particularly if either action by the oligopolist or characteristics of the industry create difficulties for entrance by others into that segment. If more than one oligopolist has dominance, each in a separate segregable part, and each abstains from entering the sub-market of the others, they may be collectively charged with conspiracy to monopolize (or conspiracy to restrain trade) by allocating the industry or allocating leadership therein.[21] Thus far, however, no Sherman Act case has invoked the concept of monopolization to cover shared power that was neither segmented into single-firm power nor aggregated as combination or conspiracy. Consequently, much of the development of oligopolies has been beyond the reach

of Section 2.

Crucial to all such cases, as well as to many that have no such broad significance, is definition of the relevant market. The boundaries of such a market can be found in any legal privilege, difference in product or service, difference in the nature of the transaction, difference in the kind of customer served, or other difference that is important enough to be a substantial obstacle to competition between persons who might significantly compete if they were not on opposite sides of the boundary between them.[22]

In spite of the Alcoa decision, restrictive conduct has continued to be important in monopolization cases. The concept of monopolization includes three variables, the market, power in it, and action to get or keep the power. There is a trade-off between the third variable and the other two. If the market is clearly identified and the power in it unmistakeable, the requisite action may be as far from inherently restrictive as that of the aluminum and shoe machinery cases. If the power is in doubt or there is doubt about the separate existence or the scope of the market in which that power is exercised, action more clearly adequate to demonstrate a monopolistic purpose may be needed to prove that there is monopolization. Restriction can show that the firm applying it has power. Thus it can establish that there is monopoly where percentages of the market are not conclusive. Similarly, where the existence of the relevant market is doubtful or the size of it is uncertain, restrictive conduct may be important in identifying it. A firm cannot exclude competitors from access to a kind of business over which it has no control, and cannot

subject customers to onerous prices or terms if they can accept better alternatives from others. Thus, when a firm applies exclusionary or exploitative restrictions, the fact that it does so indicates that there are obstacles to effective competition, and the extent of the business as to which it does so indicates the location of these obstacles and thus defines the boundaries of a market.

Few cases involve power as unquestionable as in the Alcoa case. Many, particularly those that concern regional or local monopolies, must cope with uncertainties about the scope of the market or the strength of the obstacles to broader competition which give that market identity. Restrictive conduct, particularly when it is exclusionary, is important in these cases. The concept that is relevant to them is that of the second tobacco case, that there is monopoly where there is power to exclude actual or potential competition and purpose to exercise that power.[23]

Application of this concept in regional and local settings has resulted in monopoly cases focussed chiefly upon obstacles to entry into markets, with the intent of the firm that strengthened the obstacle as a significant part of the case. In particular instances, they have identified such obstacles as tying agreements,[24] exclusive dealing arrangements,[25] five-year contracts covering an important buyer's full requirements,[26] sales commissions,[27] and group boycotts.[28]

They have also condemned under Section 2 a regionally dominant supplier's coercion of retailers to accept consignment contracts,[29] and concerted use of lawful local monopolies to expand control over other localities by using leverage in negotiating for supplies.[30]

Such applications of the law often have involved charges under both Section 2 and Section 1 (the Section covering restrictive agreements), sometimes with and sometimes without clear distinction in the decisions as to the applicability of each Section. Their practical effect has been to give Section 2 pervasive impact upon localized restrictive conduct by dominant firms. In a private suite the Supreme Court summarized this impact as follows: "There is actionable wrong whenever the restraint of trade or monopolistic practice has an impact on the market; and it matters not that the complainant may be only one merchant."[31] Similarly, in another private suit, the Court said, "Monopoly can as surely thrive by the elimination of such small businessmen, one at a time, as it can by driving them out in large groups. In recognition of this fact the Sherman Act has consistently been read to forbid all contracts and combinations 'which tend to create a monopoly', whether 'the tendency is a creeping one' or 'one that proceeds at full gallop'."[32]

<u>Attempt to Monopolize</u>.

The prohibition of attempt to monopolize obviously condemns monopolies that are not yet consummated and thus discourages would-be monopolists from formulating monopolistic plans and beginning to execute them. In most instances in which allegation of such an attempt is included in a proceding by the Government, the allegation is accompanied by other allegations -- monopolization, conspiracy to monopolize, and/or conspiracy to restrain trade. If, in a criminal case, the allegation of attempt is proved along with other allegations, penalties can be imposed for the attempt as well as for the other offenses, and the total penalty can be thus made more severe. But in a

civil case, it is highly unlikely that the judge could make any corrective order for the attempt that he could not make for the monopolization. There is also a possibility where there are multiple charges that evidence inadequate to prove that monopolization has been accomplished will be deemed adequate to prove that it has been attempted. Thus, in a case brought by the Government, multiple allegations that include allegations of attempt can serve a real but only a limited purpose.

Most cases of this kind, however, are ill-suited to establish the meaning and limits of this offense. The evidence seldom distinguishes clearly among the allegations that it is intended to support; and if more than one allegation is proved, relevant judicial opinions are likely to be concerned with major points of controversy in the case, and these are unlikely to be focussed upon differentiation of the offenses. Hence the relevant opinions in such cases seldom segregate precisely the boundaries of the proved offenses. Opinions abound in dicta about attempts to monopolize - that is, in statements that were not necessary elements of the reasoning by which the judge reached his conclusions. But these opinions are reliable guides to the meaning of the offense in only a few cases: a) those in which, though the case included multiple allegations, the allegation of attempt to monopolize was the only one that was proved or that survived some intermediate judicial winnowing, and b) those in which the only allegation was that there had been such an attempt.

Cases concerned with attempt to monopolize are numerous, but most of them are private suits. This fact, too, has retarded formulation of the law's meaning. Whereas proceedings by the Government originate in a coherent and presumably unbiased purpose to apply the law,

and express the policy and meaning of the law as interpreted by a single prosecuting authority, private suits are not similarly reliable in purpose and coherent in analysis. A private litigant who proves that he was victimized by an attempt to monopolize can recover three times the amount of his damage.[33] Thus lured toward litigation, some firms sue on dubious grounds; some sue in hope of profitable compromise in a settlement out of court, and some sue to reduce the impact of rough competition or rough bargaining that they encounter from other firms with which they compete or deal. The allegations in the suits are formulated by members of the private bar who differ in sophistication and skill, and are not subject to any central interpretative coordination. For such reasons, the allegations in the private suits differ widely in their persuasiveness as interpretations of the law and as generalizations appropriate to the facts that allegedly support them. Decisions in these private cases are formulated by numerous district court judges and, if appealed, are reviewed by several circuit courts. Since litigation is expensive and the private purposes of the suits often are achieved or thwarted before the legal issues have been authoritatively decided, few of these cases are appealed to the Supreme Court, and since that Court's work must be highly selective, still fewer attain hearing and decision there. Under such conditions, conflicting interpretations of the law are unusually likely to develop, with unusual delay in eliminating them by appellate procedures.

The meaning of attempt to monopolize was formulated as early as 1905 by the Supreme Court in a case about Swift and Co.[34] The decision said: "Intent is...essential to such an attempt. Where acts are not sufficient in

themselves to produce a result which the law seeks to prevent - for instances, the monopoly - but require further acts in addition to mere forces of nature to bring that result to pass, an intent to bring it to pass is necessary in order to produce a dangerous probability that it will happen...But when that intent and the consequent dangerous probability exist, (Section 2)...directs itself against that dangerous probability as well as against the completed result."

This statement set forth what has evolved into the so-called classical version of the law about attempt. In this version, as now applied, the offense has four elements: a relevant market, intent to monopolize it, acts that express that intent, and dangerous probability of success. Cases decided by the Supreme Court in 1951 and 1973 illustrate this classical version. In the first of these, as publisher of the only daily newspaper in Lorain, Ohio, the Lorain Journal had a monopoly there of both news and advertising. A radio station was established in a near-by town. Then the Journal refused to accept advertising by any merchant in Lorain who advertised through the radio station. The evidence showed that the purpose was to destroy the radio station, but at the time of the suit that station still existed. The Court decided that "a single newspaper, already enjoying a substantial monopoly in its area, violates the 'attempt to monopolize' clause of Section 2 when it uses its monopoly to destroy threatened competition."[35]

In the second case, Otter Tail was possessor of an exclusive franchise for distribution of electricity at retail in many small towns, and of the only transmission line that reached some of these towns.[36] Some of the towns that

wanted to establish municipal systems for distributing electricity asked Otter Tail to sell them power wholesale or use its lines to deliver to them power that they would buy from other sources. Otter Tail refused. The Court held that Otter Tail's use of control of transmission to prevent competition was an attempt to monopolize these towns.

Though used as a basis for decision in many private suits, the classical version of attempt has been sharply criticized as too narrow, and has not been invariably followed by the courts. The criticism has had both conceptual grounds and grounds that important uses of power by single firms are not covered.[37] The conceptual weaknesses are said to be a) that the concept of dangerous probability of success is applicable only where the defendant has so much power that his offenses could be easily reinterpreted as monopolization consisting of abuse of monopoly power by effort to extend it or maintain it; and b) that, since an offender will seldom if ever state explicitly an unlawful purpose, the requisite specific intent to monopolize is normally an interpretative conclusion from objectionable acts, as to which a law so formulated as to condemn such acts directly, either outright or under specified conditions, would be clearer, more likely to be consistently applied, and less likely to be biased by emotional appraisal. The inadequacies of coverage allegedly consist of imposition of impossible burdens of proof upon injured parties, and consequent unavailability of remedy where one is needed. A cited example is a case in which a wholesaler supplying nursery lamps to Sears Roebuck was required by Sears, in order to keep Sears' orders, to stop selling such lamps to Sears' competitors and, when he then refused to reduce his contract price, was subjected to predatory practices.[38] The trial court dismissed the charge, holding that "the

action taken to ruin the plaintiff and discipline suppliers may be reprehensible but there is not the slightest showing of impending monopoly." The circuit court affirmed the action on the ground that absence of proof of Sears' market power precluded a finding of attempt to monopolize.

One critic of the classical version has classified into five types instances in which it is said to be inadequate or its requirements are said to be excessive.[39] These are:

1. Deliberate price predation, practiced on a smaller firm by a substantial firm that is not the largest, in an effort to destroy it or absorb its customers.

2. Reprehensible behaviour by two or more leading firms, comparable in size, that act without agreement.

3. Effort to enforce a patent fraudulently obtained.

4. Distribution by a large supplier in which it undersells its distributor-customers.

5. Use of reciprocity by firms where they do not dominate their markets or where the so-called market consists of actual and potential customers of the firm involved.

In private suits that alleged attempt to monopolize, not all circuit courts have interpreted the law in ways consistent with the classical version of its meaning. Though all have continued to require a showing of specific intent to monopolize and improper activities expressing that intent, some have not required that a specific market be defined nor that the defendant's power in that market be shown. The

leading case of this type is a decision by a circuit court in a triple damage suit against Tidewater Oil Company that grew out of a contract between Tidewater and an operator of one of its service stations.[40] The district court had withdrawn from the jury the charge that Tidewater had attempted to monopolize. The circuit court, one judge dissenting, reversed and remanded, and then denied a petition for rehearing. The court held that "the essence of monopoly is power to control prices and exclude competition" and that there was evidence that Tidewater "possessed the specific intent to acquire and exercise that power with respect to a part of commerce...We reject the premise that probability of actual monopolization is an essential element of proof of attempt to monopolize...the specific intent itself is the only evidence of dangerous probability the statute requires - perhaps on the not unreasonable assumption that the actor is better able than others to judge the practical possibility of achieving his illegal objective." It also held that: "When the charge is attempt (or conspiracy) to monopolize, the relevant market is 'not in issue' ...a dominant position in the business of distributing petroleum products and TBA was not necessarily prerequisite to ability to monopolize an appreciable segment of interstate sales in such products. If the jury found that Tidewater intended to fix the price at which 2700 independent service station operators resold gasoline, and to exclude other suppliers of petroleum products and sponsored TBA items from competing for the patronage of these operators, and took steps to accomplish that purpose, it could properly conclude that Tidewater attempted to monopolize a part of interstate commerce in violation of Section 2 of the Sherman Act."[41]

A third interpretation of the law of attempt has developed. In this version, proof must include definition of a relevant market and intent

to monopolize it, but need not include proof that there is dangerous probability of success. This interpretation was explicit in two cases in Maryland.[42] In the first, in dismissing plaintiff's claim for failure to prove specific intent to monopolize, the district judge said that the intent which must be shown was to attain such control of a relevant market as to be able to set prices and exclude competition there, and that showing of intent to exclude competition from only part of the relevant market was not sufficient. The court distinguished between intent that was monopolistic and mere rough competition, and found the latter inadequate to show the forbidden intent. After the decision had been affirmed on appeal, the same judge decided for the plaintiff in the second case, holding that acquisition of eight establishments in Baltimore by the largest bowling chain from its nearest competitor showed intent to monopolize a defined market, but that proof of dangerous probability of success was not necessary.

These conflicting interpretations have not yet been reconciled by the Supreme Court. The Classical version of the law of attempt appeared in that Court's decisions in the Lorain Journal and Otter Tail cases, as noted above, and the Court has denied certiorari repeatedly in private cases in which lower courts applied the same version.[43] However, it also denied certiorari in the two cases in which the decision had expressed a different interpretation.[44]

Two suits by the Government, now awaiting trial, should help to clarify the law if they are decided and appealed. These are cases, substantially parallel in content, filed in 1973 against Goodyear and Firestone.[45] Each alleges that the company has attempted to monopolize the manufacture and sale of replacement tires. (Each case also includes a charge that specified acquisitions by the

company have violated Section 7 of the Clayton Act.)

According to the complaints, Goodyear and Firestone are respectively the largest and second largest rubber fabricators in the world, and respectively the largest and second largest makers of tires in the United States. Goodyear's sales are more than $4 billion yearly; Firestone's "at least" $2.5 billion. Goodyear's assets are more than $3 billion; Firestone's "at least" $2.25 billion. The two companies rank respectively nineteenth and thirty fourth in sales among United States industrial corporations. Each distributes tires partly through company-owned stores: about 1,400 for each. Goodyear makes 30 per cent of original equipment tire sales, Firestone 27 per cent. In unit sales, Goodyear has 28 per cent of the replacement tire market, Firestone more than 25 per cent. Each has grown since 1959 in its share of the latter field - Goodyear from 23 per cent to 28 per cent, Firestone from 15 per cent to 25 per cent.

There are three other major American makers of tires. The five majors sell "over" 95 per cent of original equipment tires for passenger cars, and "over" 80 per cent of replacement tires for such cars. By deducting the percentages attributed to Goodyear and Firestone I infer that the total for the other three is somewhat more than 38 per cent for original equipment and 27 per cent for replacement. No new maker of tires has entered the industry since the 1930's. Of the 13 tire makers other than the majors that existed in 1959, three had been driven out of business by 1967, the defendants having each acquired one of them, and a fourth, with a much reduced market share, was selling a third of its production to Firestone.

The attempt to monopolize that is charged in this setting of great size and growing concentration consists of a) substantial reduction in 1959 by Goodyear of the prices of passenger tires for replacement, and similar reduction in 1960 by Firestone; b) maintenance of low prices by both until 1966 to weaken smaller competitors; c) arrangement with more than 10 oil companies by Goodyear and with more than 16 by Firestone for commissions on tires, batteries, and accessories that were coercive upon the service stations of those oil companies, thus foreclosing these stations as markets for smaller tire manufacturers; d) use of reciprocal dealing programs to get business at the expense of smaller firms with less buying power; e) specified acquisitions (a competitor by Goodyear, many wholesale and retail distributors and some facilities of competitors by Firestone); f) significant increase of tire prices from 1966 onward. The complaint against Firestone added an additional means, - a requirement contract that tied to Firestone a substantial part of the capacity of one independent producer.

Monopolization, Attempt, and the Federal Trade Commission Act.

Underlying the controversy over the meaning of attempt to monopolize is an unresolved difference of opinion as to the conditions under which American antitrust law can and should be applied to anticompetitive practices by powerful firms. The classical version of attempt law gives Section 2 of the Sherman Act very limited functions as a remedy for such practices. The alternative interpretations give it a considerably wider one. One commentator, thinking the task of curbing such practices too formidable for judicial application of a criminal law, lists numerous types of practice that he considers

potentially vulnerable under a broad interpretation, and argues that under such an interpretation desirable conduct might be forbidden by judicial decree founded on mistaken diagnosis, and even more such conduct might be deterred by uncertainty about the legal risks involved.[46]

When the Sherman Act is used to explore the numerous problems that are involved, the stakes are high. Whatever is contrary to that Act is a criminal offense, subject both to punishment and to private suits in which triple damages may be recovered. Use of Section 5 of the Federal Trade Commission Act for similar exploration is an alternative in which the potential of the law is broader and the stakes are lower. The Commission may use its authority not only to require that practices violative of the Sherman Act be stopped, but also to impose a similar requirement upon incipient violations of that Act and upon practices that are contrary to the policy of that Act.[47] Its orders cover future conduct and may cover future business structure, but cannot impose penalties for what has passed, and its decisions do not give injured persons rights to triple damages.[48]

These differences have practical effects, derived from the fact that the Commission's focus is not upon intent but upon effect upon competition. A complaint by the Commission in 1971 alleged in two counts that acquisitions by Golden Grain, a macaroni company, violated Section 5 of the Federal Trade Commission Act.[49] Count I specified that the acquisitions were an attempt to monopolize sales of dry paste products in the Pacific Northwest. Count II specified that they were unfair methods of competition. In deciding the case, the Commission dismissed Count I. It decided that the evidence tended to show that "it was not the respondent's sole purpose to gain monopoly power," though that

might have been "the overriding purpose," and that "the mere showing that the acquisitions were made....is not evidence, standing alone, from which we can infer specific intent." However, the Commission issued an order under the second count. Considering three acquisitions, it held that one of them was "a potential means of monopolization or further substantial lessening of competition"; a second was "contrary to the intent and policy of the Clayton Act" and "anticompetitive to a substantial degree," and a third, a dominant firm's acquisition of a small competitor in a concentrated market, was of a kind that "may substantially lessen competition."

Citing this and other cases, the director of the Commission's Bureau of Competition concluded that "Section 5 of the FTC Act proscribes all unfair methods of competition, including single-firm anticompetitive behavior which would not amount to a violation of Section 2 of the Sherman Act ... Under Section 5, a firm need not to be dangerously close to becoming a monopolist...it need only possess the power and resources to hinder or stifle competition and be found to have taken unfair actions to achieve that end."[50] He used as examples two hypothetical restrictions: a) temporary selective low prices and high promotional expenditures, financed by diversion of resources from the firm's other markets, and b) a selective supply squeeze imposed in time of shortage by a vertically integrated firm upon an important competitor-customer.

Whether or not Section 5 can be used for comprehensive consideration of the structure and conduct of an oligopolistic industry is now being determined in what appears to be a test case as to ready-to-eat (RTE) cereals.[51] This case seems to be potentially so significant that what follows will examine it in considerable

detail.

A single complaint charges that the four largest manufacturers of such cereals each have "engaged in acts or have practiced forbearance with respect to the acts of other respondents, the effect of which has been to maintain a highly concentrated, non-competitive market structure in the production and sale of RTE cereals." The complaint alleges no agreement among the four, and thus differs sharply from a charge that might support an allegation of conspiracy to monopolize or to restrain trade under the Sherman Act.

Listed in the order of their domestic sales of RTE cereal, and described as they were in 1970, the respondents are: 1) Kellogg, ranked 191st in sales among the 500 largest industrial corporations, with assets of $347 million and sales of $614 million, with domestic sales of RTE cereal of $300 million; 2) General Mills, ranked 116th of the 500 largest, with assets of more than $665 million and sales of more than $1 billion, with domestic sales of RTE cereal of $141 million; 3) General Foods, ranked 45th of the 500 largest, with assets of more than $1.3 billion and sales of more than $2 billion, with domestic sales of RTE cereal of $92 million; 4) Quaker Oats, ranked 195th of the 500 largest, with assets of more than $391 million and sales of $597 million, with domestic sales of RTE cereal of $56 million. The advertising expenditures of these four for RTE cereal were, respectively, $36 million, $19 million, $9 million, and $9 million.

The complaint does not name Nabisco and Ralston Purina as respondents, though it says that each of them participated in some of the acts that it alleges. It gives figures for each: for Nabisco, ranked 140th of the 500, assets of more than $503 million, sales of

more than $868 million, of which domestic sales of RTE cereal were $26 million; for Ralston, ranked 71st of the 500, assets of more than $775 million, sales of more than $1.5 billion, of which domestic sales of RTE cereal were more than $20 million. The cereal advertising expenditures of Nabisco are given as $3 million; those of Ralston as more than $4 million.

The acts and forbearances, as specified in the complaint, are as follows:

1. Brand proliferation and product differentiation. Respondents have introduced from 1950 to 1970 about 150 brands, more than half of them since 1960. They use intensive advertising, directed particularly at children, to promote trademarks that conceal the true nature of the products. They artificially differentiate cereals that are basically similar, emphasizing trivial variations. They use premiums to induce purchasing. During the period 1950-1970 they increased aggregate expenditures for advertising from $26 million to $81 million, and in 1970 spent 13 per cent of receipts from sales on advertising.

2. Misrepresentation. a) they all represent that their cereals, without other foods, enable children to perform physical activities represented or implied in their advertising, whereas this is not so. b) The first three of them represent that consumption of RTE cereal at breakfast will reduce body weight without adherence to a reduced calorie diet; maintain body weight even if caloric intake increase, and will do one or the other without regular exercise. c) The first two of them also represent that failure to eat one of their cereals results in failure to perform to full capability, and that its ingestion results in better performance.

Such misrepresentations facilitate artificial differentiation of products and brand proliferation, and enhance ability to charge monopoly prices and exclude competitors.

3. Control of shelf space. Kellogg's control of shelf space in retail outlets interferes with marketing efforts by others. Kellogg uses it to protect and perpetuate the respective market shares of the four, and the others acquiesce.

4. Acquisitions. Significant sources of private label cereal have been eliminated by acquisitions, and the shared monopoly structure of the industry has been thus enhanced. Acquisitions explicitly mentioned are two by General Foods and one by Kellogg.

5. Forbearance. Each respondent has refrained from challenging decisions by the others to increase prices, and has acquiesced in or followed such increases; has restricted use of trade deals and promotions directed at the trade, and has limited the use of promotions directed at consumers, such as coupons, premiums, and cents-off deals.

By such means, the complaint says, each respondent has exercised monopoly power. They have individually and collectively inflated prices artificially; obtained profits greater than they would have obtained in a competitively structured market; supplanted product innovation by product imitation; lessened actual and potential competition, and blockaded entry. Individually and in combination, they have maintained a highly concentrated non-competitive market structure; obtained, shared, and exercised monopoly power; and raised barriers to entry by unfair methods.

The order proposed in the complaint would include divestiture of plants and other facilities, royalty-free licensing of trademarks for a specified period, prohibition of acquisition of cereal manufacturers, and prohibition of provision of shelf-space services.

If this complaint results in an order that is sustained, the importance of the decision will depend upon its conceptual focus. Though the complaint does not charge the companies with restrictive agreement, it does allege mutual forbearance, acquiescence in price increases, imitation of them, and "collective" artificial inflation of prices. If in the decision agreed action is distilled from this language, the case may eventually help decide the legal boundaries of restrictive agreement. If, however, the companies are found to have violated the Act by parallel individual action, the Federal Trade Commission Act will be a new legal tool against oligopolies.

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Footnotes

1. The three largest tobacco companies, for example, were convicted in the 1940's of all three offenses, monopolization, attempt to monopolize, and conspiracy to monopolize, and were also convicted under Section 1 of the Sherman Act of conspiring to restrain trade. See American Tobacco Co. v. U.S., 328 US 781 (1946).

2. U.S. v. Yellow Cab Co., 332 US 218 (1947). See also U.S. v. Consolidated Laundries Corp., 291 F. 2d. 563 (2nd Circuit, 1961).

3. Standard Oil Co. of New Jersey v. U.S., 221 US 1 (1911).

4. U.S. v. United States Steel Corp., 251 US 417 (1920).

5. U.S. v. Swift & Co., 286 US 106 (1932).

6. U.S. v. Aluminum Co. of America, 148 F. 2d. 416. This was the final decision of the case. For lack of a quorum of judges that were not personally disqualified, the Supreme Court had referred the case to the circuit court of the Second Circuit for disposition. In subsequent cases, the Supreme Court endorsed the views expressed in the opinion; See American Tobacco Co. v. U.S., op. cit., note 1.

7. In the Grinnell case (U.S. v. Grinnell, et. al., 236 F. Supp. 244 (D.C.R.I., 1964)), the judge said, "once the Government has borne the burden of proving what is the relevant market and how predominant a share

of that market defendant has, it follows that there are rebuttable presumptions that defendant has monopoly power and has monopolized in violation of Section 2...defendant... is free...to maintain the burden of showing that its eminence is traceable to such highly respectable causes as superiority in means and methods which are 'honestly industrial'."

In the nine cases in which the Supreme Court has confirmed a finding of monopolization, the lowest percentage of the market held by the defendant was 70. See U.S. v. Paramount Pictures, Inc., 334 US 131 (1948).

8. See Hughes Tool Co. v. Cole, 113 F. Supp. 519 (W.D. Okla., 1953), affirmed 215 F. 2d. 924 (10th Circuit, 1954), certiarari denied, 348 US 927 (1955).

9. U.S. v. United Shoe Machinery Corp., 110 F. Supp. 295 (D. Mass., 1953), affirmed per curiam 347 US 521 (1954). The company had achieved its dominance partly by a combination of separate companies (which the Supreme Court had found lawful in 1918) and partly by patenting the results of its own research; but the fundamental patents had expired.

10. Standard Oil Co. of New Jersey v. U.S., <u>op. cit</u>., note 3.

11. U.S. v. Grinnell Corp, <u>et al</u>., 384 US 563 (1966).

12. U.S. v. E.I. duPont de Nemours & Co., 351 US 377 (1956).

13. U.S. v. International Business Machines Corp., 13 F. Supp. 11, (S.N.N.Y. 1935), affirmed 298 US 131 (1936).

14. Civil Action 72-344.

15. The 1973 decision in Honeywell, Inc., v. Sperry-Rand Corp., _et al_., appears on pp. 5794-5920 of _The Industrial Reorganization Act_, Hearings Before the Sub-committee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 93rd Congress, 2nd Session, on S. 1167, Part 7, The Computer Industry (hereafter called Hearings).

16. Hearings, _op. cit_., Note 15, pp. 5708-5709.

17. The complaint appears in _ibid_, pp. 5488-5499; the content of the settlement is described in _ibid_, pp. 5292-5293 and 5297.

18. _Ibid_, pp. 5709-5794.

19. U.S. v. International Business Machines Corp., Civil Action No. 69-200, filed Jan. 12, 1969. The complaint appears in _ibid_, pp. 5699-5702, and two accompanying memoranda, one about requested relief, on pp. 5703-5708.

20. Cf. Corwin D. Edwards, "Policy Toward Big Business: What Lessons After Forty Years?", 9 _Journal of Economic Issues_ 343 (1975), at 349-350. Cf. also Corwin D. Edwards, "Economic Concepts and Antitrust Litigation: Evolving Complexities", 19 _Antitrust Bulletin_, 295 (1974), at 306-308.

21. The case by the Federal Trade Commission against the cement industry's use of a multiple basing-point system (see Chapter 1V on systematic delivered pricing) could have been, and sometimes was, described as such a conspiracy to allocate leadership. Since it was brought under Section 5 of the Federal Trade Commission Act, the niceties

of interpretation of the Sherman Act that are relevant here were not there pertinent. Charges under Section 1 of the Sherman Act may be brought against monopolists in industries in which control has not been segmented, if the activities of these firms are so coordinated and the coordination has been so achieved that the result amounts to what the Sherman Act calls combination or conspiracy and what the Federal Trade Commission calls a planned common course of action. But much of oligopolistic action, though significant, falls short of so much coordination.

22. Championship boxing contests, as distinguished from all such contests, were held to be a relevant market in International Boxing Club of New York v. U.S., 358 US 242 (1959).

23. American Tobacco Co. v. U.S., op. cit., note 1.

24. Northern Pacific Railway Co. v. U.S., 356 US 1 (1958).

25. F.T.C. v. Motion Picture Advertising Service Co., 344 US 392 (1953). Though this decision pertained to Section 5 of the Federal Trade Commission Act, its substance pertained to violation of that Act by conduct violative of the Sherman Act.

26. U.S. v. American Can Co., 87 F. Supp. 18 (1949). In this case the court required that the duration of such contracts be not more than one year.

27. Atlantic Refining Co. v. F.T.C., 381 US 357 (1965). This case, too, interpreted Section 5 of the Federal Trade Commission Act as to conduct violative of the Sherman Act.

28. Klors, Inc. v. Broadway-Hale Stores, Inc., 359 US 207 (1959).

29. Simpson v. Union Oil co. of California, 377 US 13 (1964).

30. U.S. v. Griffith, 334 US 100 (1948).

31. Simpson v. Union Oil Co. of California, op. cit., note 29.

32. Klors, Inc. v. Broadway-Hale Stores, Inc., op. cit., note 28. It is noteworthy that in thus stressing tendency the Court has given the Sherman Act a stretch to cover incipient conditions similar to the scope of Section 5 of the Federal Trade Commission Act; but the significance of this fact may be reduced by the fact that the case was one about group boycott, involved charges under both Section 2 and Section 1, and involved allegations of both monopolization and attempt to monopolize. The language of the relevant part of the opinion does not distinguish the Sections or the charges.

33. Section 4 of the Clayton Act. Before 1914, a similar right was provided by Section 7 of the Sherman Act, which was repealed in 1955.

34. Swift & Co. v. U.S., 196 US 375 (1905).

35. Lorain Journal Co. v. U.S., 342 US 143 (1951).

36. Otter Tail Power Co. v. U.S., 410 US 366 (1973).

37. Two good examples of such criticism are Paul E. Levine, "Attempt to Monopolize Under the Sherman Act: Defendant's Market Power as a Requisite to a Prima Facie Case",

73 Columbia Law Review 1451, and Edward H. Cooper, "Attempts and Monopolization: A Mildly Expansionary Answer to the Prophylactic Riddle of Section Two", 72 Michigan Law Review 375.

38. Mackey v. Sears, Roebuck & Co., 237 F. 2d. 869 (7th Circuit, 1956); petition for certiarari dismissed by stipulation, 355 US 865 (1957). In the words of the director of the Commission's Bureau of Competition, "one is left with the impression that the 'dangerous probability' requirement in attempt cases may tend to a dangerous probability that anticompetitive practices, more often than not, may escape the reach of Sherman 2."

39. Cooper, op. cit., note 37. The language in which the types are summarized here deviates from Mr. Cooper's in an effort to shorten definitions of types and, in one or two instances, to sharpen his apparent meaning.

40. Lessig v. Tidewater Oil Co.. 327 F. 2d. 459 (9th Circuit, 1964), certiorari denied, 377 US 993 (1964).

41. A similar interpretation was expressed in a different circuit, in a case involving different facts, in Mt. Lebanon Motors, Inc., v. Chrysler Corp., 283 F. Supp. 453 (W.D. Penna., 1968), affirmed per curiam, 417 F. 2d. 622 (3rd Circuit, 1969). Chrysler had established factory dealerships which cut prices and advertised massively, and allegedly operated below cost. An independent franchised dealer charged the company with monopolization and attempt to monopolize. The trial court directed a verdict of acquittal on the charge of

charge of monopolization because of Chrysler's competition with Ford and General Motors, but denied Chrysler's request for such a verdict on the charge of attempt on the ground that, regardless of market power, attempt covered acts with intent to monopolize.

For similar interpretations see also Union Carbide & Carbon Corp. v. Nisley, 300 F. 2d. 561 (10th Circuit, 1961); Rea v. Ford Motor Co., 355 F. Supp. 842 (W.D. Penna., 1973); and Hallmark Industry v. Reynolds Metals Co., CCH, 1973-2 Trade Cases #74,828.

42. American Football League v. National Football League, 205 F. Supp. 60 (D. Md., 1962), affirmed 323 F. 2d. 124 (4th Circuit, 1963) and Bowl America, Inc. v. Fair Lanes, Inc., 299 F. Supp. 1080 (D. Md., 1969). See also Kearney & Trecker Corp. v. Gidding & Lewis, Inc., 452 F. 2d. 579 (7th Circuit, 1971), certiorari denied, 405 US 1066 (1972).

43. Panotex Pipe Line Co. v. Phillips Petroleum Co., 457 F. 2d. 1279 (5th Circuit,1972), certiorari denied 409 U.S. 845 (1972); Cornwell Quality Tools Co. v. C.T.S. Co., 446 F. 2d. 825 (9th Circuit, 1971), certiorari denied, 404 US 1049, (1972); Bernard Food Industries, Inc. v. Dietene Co., 415 F. 2d. 1279 (7th Circuit, 1969), certiorari denied, 397 US 912 (1970).

44. The Tidewater Case (see note 40) and the Kearney Case (see note 42).

45. U.S. v. Goodyear Tire and Rubber Co., Civil No. C-73-835, August 9, 1973 and U.S. v. Firestone Tire and Rubber Co., Civil No.

C-73-836, August 9, 1973.

46. Cooper, op. cit., note 37. The types of practice listed include predatory pricing and refusals to deal, both discussed at some length on pages 435-445 of Mr. Cooper's article, and also the following types, listed and accompanied by footnote references to cases, but not otherwise discussed: a) physical violence to competitors, their customers, or their products; b) predatory spending upon fighting brands or dummy independent firms or upon new facilities, new products, advertising, or expansion; c) price discrimination in selling or exaction of special advantage from suppliers; d) acquisition of competitors or of suppliers or customers or of facilities to be closed down; e) misuse of patents, copyrights, or trademarks, or misuse of litigation about other types of rights; f) subversion of governmental regulatory programs; g) interference with the advantageous relationships of other firms directly, by misrepresentation or disparagement, by surveillance, or by advance announcement of new products well before they are actually available; h) preclusion of competitive opportunities by exclusive dealing requirements, tying arrangements, designing accessories so that they require integral use, influencing buyers to adopt restrictive specifications for products, threatening to compete with customers who buy from rivals, or obtaining covenants against competition or against revelation of competitive information.

47. Fashion Originators Guild of America v. F.T.C., 312 US 457 (1941); F.T.C. v. Motion Picture Advertising Service Co., Inc., 344 US 392 (1953); F.T.C. v. Brown Shoe Co., Inc., 384 US 316 (1966).

48. A private litigant, of course, may benefit from the facts and decisions of cases decided by the Commission, but he bears the burden of proving that violation of the Sherman Act or the Clayton Act was involved and that thus Section 4 of the Clayton Act is applicable.

49. In the Matter of Golden Grain Macaroni Co., 78 FTC 63, (1971), at 165. See also Golden Grain Macaroni Co. v. F.T.C., 1973 Trade Cases, #74,300 (9th Circuit, 1972).

50. James T. Halverson, "FTC Antitrust Enforcement Policies: Multi-firm and Single-firm Problems Deriving from Abuses of Various Forms of Market Power", Address before the Ohio Legal Center Institute, Columbus, Ohio, June 21, 1974 (duplicated), pp. 22-23.

51. Docket 8883: In the Matter of Kellogg Co., General Mills, Inc., General Foods Corp., and the Quaker Oats Co., Complaint April 26, 1972. Statements from the Commission indicate that similar action is being considered as to other fields: office copiers, lumber, and petroleum. (See Halverson, op. cit., note 50, p.1.) On June 13, 1975, a news release by the Commission said that it had opened an investigation into the structure, conduct, and performance of firms manufacturing and selling soap and detergents, with primary attention to heavy-duty detergents.

APPENDIX

THE CONTENT OF THE ANTITRUST LAWS

The right of the Federal Government to act against impairments of competition is derived chiefly from the constitutional provision by which it may regulate interstate commerce. (There are other bases for Federal control, such as the power to levy taxes, but in control of restrictions they have been relatively unimportant; they will be disregarded here.) Federal authority can prevent and punish restrictions of interstate commerce by private persons or organizations. If a state government restricts interstate commerce by its law or policy, Federal law can set the restriction aside so far as the Federal Government chooses to act against it.

Federal authority extends over restrictions that, though intrastate in character, directly affect interstate commerce. As the economic integration of the country has grown, the field in which the effect of restrictive action is merely intrastate has diminished, so that today almost any restriction that is big enough to be important is probably under Federal jurisdiction.

Nevertheless, reliance upon interstate effect as a basis for Federal action sometimes has bizarre effects, when applied to localized restrictions. When such restrictions are applicable to commodities not locally produced - for example, price fixing undertaken by local distributors of paint - they are likely to be regarded as subject to Federal jurisdiction on the ground that the local restriction impairs the flow of that paint to

the locality from makers in other states. Related restrictions upon locally produced services - for example, agreements to fix charges for local painting contracts made by local contractors who buy the paint from local distributors - are likely to be conceived as intrastate, on the ground that the paint had come to rest within the state before the contractors acquired it. Yet an analogous agreement about contracts to lay tile, made by local tile contractors, may be considered subject to Federal jurisdiction because the tile contractors, unlike the paint contractors, had not bought their tile locally. Numerous similar distinctions, derived from differences in the directness of an interstate effect, exist and in general tend to place services in the distribution of tangible products more fully under Federal jurisdiction than other kinds of local services.

Similarly, Federal jurisdiction is likely to reach further in localities close to the boundaries of states than in similar localities far from those boundaries. Sand and gravel produced and utilized locally may be clearly in interstate commerce in St. Joseph, Missouri, on the Kansas border, but not so in Columbia, Missouri, in the centre of the state. Since the trading area of a city tends to grow with its population, Federal jurisdiction over local action tends to be greater in the larger cities, and this difference is likely to be reinforced by the fact that in general the larger cities contain the central offices of the larger enterprises that have the greater areas of activity.

Thus, in spite of the fact that numerous local restrictions are beyond Federal control, Federal authority is so persasive that, for

most purposes, its limitations have slight practical significance.

Three broad statutes, generally applicable, constitute domestic American competition policy. The first of these, the Sherman Act, a criminal law enacted in 1890, is enforceable by fine and imprisonment, by injunctive orders, and by seizure of goods in transit. It contains two basic prohibitions. One of these forbids contracts, combinations, and conspiracies in restraint of trade. (By subsequent amendment, still highly controversial, it exempts from its prohibition resale price contracts applicable to branded goods, so far as these are lawful in the state in which the resale takes place and so far as they do not involve horizontal restrictions.) The second prohibition forbids anyone from monopolizing, attempting to monopolize, or combining with others to monopolize any part of commerce among the states or with foreign nations.

Two supplementary laws, both enacted in 1914, extend the reach of prohibitions and provide additional kinds of application. The simpler one, the Clayton Act, provides exemption for labour and agricultural organizations, and sets forth four additional general prohibitions, which have been conceived as applicable to "incipient" violations of the Sherman Act. Two of these, concerned with price discrimination and corporate acquisitions, have been substantially altered by subsequent legislation. Their content is analyzed in the chapters of this paper that are concerned with those topics. The other two, substantially unaltered since 1914, pertain to tying contracts and exclusive dealing contracts, which are prohibited where the effect "may be" to "substantially lessen competition or tend to create a monopoly in any line of commerce"; and to

interlocking directorates, which are forbidden if the interlocked corporations are competitors and any of them has an owners' equity exceeding $1 million. (The Clayton Act also contains special provisions applicable to banks and common carriers, which are relevant to Federal regulatory control over these fields, but are not summarized here.)

Enforcement of the Clayton Act is entrusted both to the Federal courts by civil proceedings that lead to judicial orders and to Federal commissions. Four of these commission, each with a field of regulatory authority (the Interstate Commerce Commission, the Federal Communications Commission, the Civil Aeronautics Board, and the Federal Reserve Board), are given jurisdiction as to parts of the Act applicable to their fields of regulation. A fifth commission, with jurisdiction over all other applications of the statute, is the Federal Trade Commission, created by the other law enacted in 1914. Violation of orders issued by any of the commissions after they become final is subject to civil penalties in the form of a fine for each day of violation.

With its subsequent amendments, the Federal Trade Commission Act establishes a five-person commission, of whom not more than three may come from the same party. They are appointed to staggered terms by the President, subject to confirmation by the Senate. The President designates their chairman. The Commission is authorized to prevent persons (other than those subject to specified types of special regulatory control by other agencies) from using unfair methods of competition in commerce or unfair or deceptive acts or practices in commerce. Its proceedings as to such matters, and also as to alleged violations of the Clayton Act, may result in orders that such activities be discontinued. Its orders become final if not

appealed, and thereafter are enforceable by civil penalties. In appeals, its findings of fact are final, though not its interpretations of law, and orders by appellate courts, when they become final, are enforceable by proceedings for contempt.

If a deceptive act consists of false advertisement of food, drugs, curative devices, or cosmetics, and may be injurious to health or is made with intent to mislead, the offense becomes a misdemeanour subject to fine in proceedings by the Attorney General or, if he does not act, by the Commission.

The Commission's role has been conceived as one of exploring the frontiers of policy. Indeed, courts have defined the Clayton Act as directed against incipient violations of the Sherman Act, and the Federal Trade Commission Act as directed against incipient violations of the Clayton Act and acts contrary to the policy of the antitrust laws. For this reason, the statute gives the Commission broad investigatory powers and broad authority to make public reports. Apart from investigation and disclosure incident to enforcement of the prohibitions that it administers, it is authorized to investigate the way in which antitrust decrees are carried out, to report its findings and recommendations to the Attorney General, and to publish them at its discretion. When directed by the President or by the Congress, it is empowered to investigate and report the facts about any alleged violations of the antitrust laws. It also has power to engage in other investigations on its own initiative. It may require corporations under its jurisdiction to file annual and special reports and answers in writing to specific questions furnishing such information as it may require about their "organization, business,

conduct, policies, management, and relation to other corporations, partnerships, and individuals." It is empowered to make public such parts of the information it obtains (except trade secrets and names of customers) as it deems expedient in the public interest. It is authorized to investigate trade conditions "in and with" foreign countries where associations, combinations, or practices of traders, "or other conditions," may affect American foreign trade. As to either its domestic or its foreign trade investigations, it may make recommendations to Congress. Governmental departments and bureaus are required, when directed by the President, to furnish to the Commission "all records, papers, and information in their possession" relating to any corporation, and to detail personnel to the Commission. Corporate refusal to answer inquiries or produce documents is an offense subject to fine and imprisonment. So are false statements of fact in reports to the Commission, false entries in or alteration of corporate records, willful failure to make full entries in such records, and willful removal of documents from the jurisdiction of the United States. Delay in filing reports required by the Commission is subjected to daily civil penalties. Unauthorized disclosure of information by Commission personnel is subject to fine and imprisonment.

Both the Federal Trade Commission and the Department of Justice have developed less formal means of attack upon their problems alongside their formal activities in legal proceedings. Both agencies negotiate with offenders for settlement of their complaints. If agreement is reached, the Commission enters a consent order; and the Department recommends to the appropriate court that the court make an order that the defendant has agreed to accept, or accept from the defendant a plea

of *nolo contendere* to a criminal charge and impose a penalty to which the defendant has agreed. In some types of cases - e.g., price discrimination complaints by the Commission - the number of consent settlements is much larger than the number of full legal contests.

Both agencies also use broader means than legal cases. In the last few years, the Commission has begun to use the rule-making power given it by the Federal Trade Commission Act to formulate trade regulation rules that, once tested by the courts, are authoritative interpretations of the laws that it administers. Both agencies have issued statements of their policies in instituting cases in particular fields, notably about mergers. Both agencies give advice to firms and groups. The Department does so only as to activities not yet undertaken; but if advice from it is requested about such an activity and accompanied by a full and candid statement about what is contemplated, the Department undertakes, if it does not then condemn the activity, to confine any later challenge of it to a civil (as distingushed from a criminal) proceeding. The Commission gives advice at two levels - formal advice by the Commission itself, the substance of which is sometimes released for publication, and less formal advice by members of the staff, expressed less precisely; such advice is not limited to activities not yet undertaken. In particular instances, the Commission accepts formal or even informal assurances by an offender that his challenged practices will cease. Where similar practices seem to be widespread, the Commission may publish an interpretative guide to the meaning of the law, either of general application or confined to the setting of a particular industry. Occasionally it holds a public hearing to discuss the application of some legal provi-

sion in some industry. It may also participate in a trade practice conference with members of an industry that results in its approval of so-called trade practice conference rules - rules that, unlike the rules mentioned above, do not have legal authority, but set forth interpretations of the law that the Commission has made after talk with the industry and with approval or acquiescense by members of the industry. Such rules sometimes include definitions of types of concerted action in the industry that the Commission has approved as desirable or harmless though not legally required.

Private persons who are injured by violations of the Sherman Act or the Clayton Act may sue in the courts for injunctions against further injury and for recovery, not of the value of damage done to them, but of three times that value. The provision for tripling the damage claim was intended to stimulate private litigation in support of antitrust policy. It has resulted in considerable numbers of private suits, and hence in need for firms to consider not only whether or not their conduct will be challenged by the Government but also whether or not it will result in private suits against them. Among the apparant by-products of such suits are a) a tendency for the risk of large private claims for damages to reinforce the relatively small public penalties as deterrents to violation, and b) a tendency to diminish the authority of the agencies of the Government responsible for the public policy of maintaining competition as interpreters of the laws in which that policy is expressed; for governmental interpretations do not control interpretations that private litigants may make and present to the courts for adjudication, and inaction by the Government, expressing policy or inertia, does not protect the beneficiaries of it from private suits.

The laws and procedures described above provide broad options. As to much of the conduct and business structure that may have anticompetitive implications, they provide more than one legal provision under which corrective action can be undertaken. Restrictive agreements - allocation of goods under specialization agreements, fixation of prices under pricing formulas, or any other kinds of concerted restriction that affect interstate commerce and are not exempted by law - are forbidden both under Section 1 of the Sherman Act and under Section 5 of the Federal Trade Commission Act. Monopolization and attempts to monopolize are unlawful under Section 2 of the Sherman Act and also under Section 5 of the Federal Trade Commission Act. Particular types of conduct are subject to attack under the relevant sections of the Clayton Act - price discrimination under Section 2, tying and exclusive dealing arrangements under Section 3, acquisitions of stock or assets of a corporation by another corporation under Section 7, and interlocking directorates under Section 8; these sections differ from one another as to the kinds of probable effect that make unlawful the conduct they specify. Everything covered by these sections, however, is also subject to attack under Section 5 of the Federal Trade Commission Act, and in such an attack many of the limitations of the similar provisions of the Clayton Act do not apply, e.g., the limitation of Section 2 (d) and Section 2 (e) of the Clayton Act so that it applies to sellers but not buyers, and the limitation of Section 7 of that Act to acquisitions in which the acquired property is corporate. Thus the Federal Trade Commission Act provides a substitute proceeding that sometimes fills gaps in the Clayton Act's prohibitions. Moreover, much of the conduct subject to the Clayton Act is subject to the Sherman Act also. This is true wherever the activity is concerted and

has actual, instead of merely probable, restrictive results. It is also true, where the activity in question is individual rather than concerted, if the restrictive results are so substantial that they amount to attempt to monopolize a part of commerce. Thus, in application of a large part of antitrust policy, the Government has available two or more provisions of law as alternatives or supplement to each other.

The alternative provisions are enforceable by different means and to different extents. The Sherman Act is a criminal statute, under which offenders can be punished by fine and imprisonment. Under it the courts can also order changes in business structure and in business conduct. The Government can proceed under it in either way or in parallel cases in both ways at once. Section 3 of the Robinson-Patman Act, also a criminal law, can be applied against some but not all kinds of price discrimination, though it is seldom used.

The Clayton Act and the Federal Trade Commission Act are not criminal laws, and contain no provisions for punishment of past offenses. Both of them can be used to control future conduct, and, to an extent not yet fully explored, the latter can be used also to change business structure. Orders under the Clayton Act develop in two ways: a) as orders by a court after a proceeding by the Department of Justice, and b) orders by the Federal Trade Commission after proceedings conducted and decided by the Commission. The latter types of orders, however, become final only if they are not appealed, and otherwise may be affirmed, modified, remanded for reconsideration, or rejected by the courts. Judicial orders under this Act can be enforced by proceedings for contempt of court; final orders

by the Commission are enforceable by civil monetary penalties for each day of violation. Orders by the Federal Trade Commission under the Federal Trade Commission Act are subject to judicial review similar to that as to the Commission's orders under the Clayton Act, except that the Commission's findings of fact, if supported by evidence, are conclusive, and the Commission's final orders under this Act are also enforceable by civil monetary penalties incurred for each day of violation.

Apart from legal proceedings that involve adversary confrontation, both the Department of Justice and the Federal Trade Commission use consent settlements - procedures in which the content of a formal order is negotiated with those against whom it is issued prior to its issuance. Orders to which the Department has agreed are submitted to the appropriate court with the Department's recommendation that the court issue them; usually but not invariably the court agrees to do so. Orders by the Federal Trade Commission are issued without judicial intervention. In both types of settlements, negotiation may take place and be successfully completed before there is a formal complaint, so that the complaint and the agreed settlement are issued simultaneously. In criminal proceedings, the Department of Justice sometimes similarly negotiates a penalty, which is recommended to the court with a statement by the defense that although guilt is not admitted the recommended penalty will be accepted.

Thus American antitrust policy includes a wide range of options as to reliance upon procedures educational or legal, broad or narrow, and corrective or punitive, to encourage compliance with the policies of the law. In the broad field in which alternative legal procedures are available, the options as to use of provisions of law frequently include options as to choice of the deciding body and as to the way in which compliance with the law shall be assured.

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